

# China Banking Outlook Lessons from Japan and Korea

中国银行业前景 -  
借鉴日本与韩国的经验

*Euromoney Global China DCM Congress*

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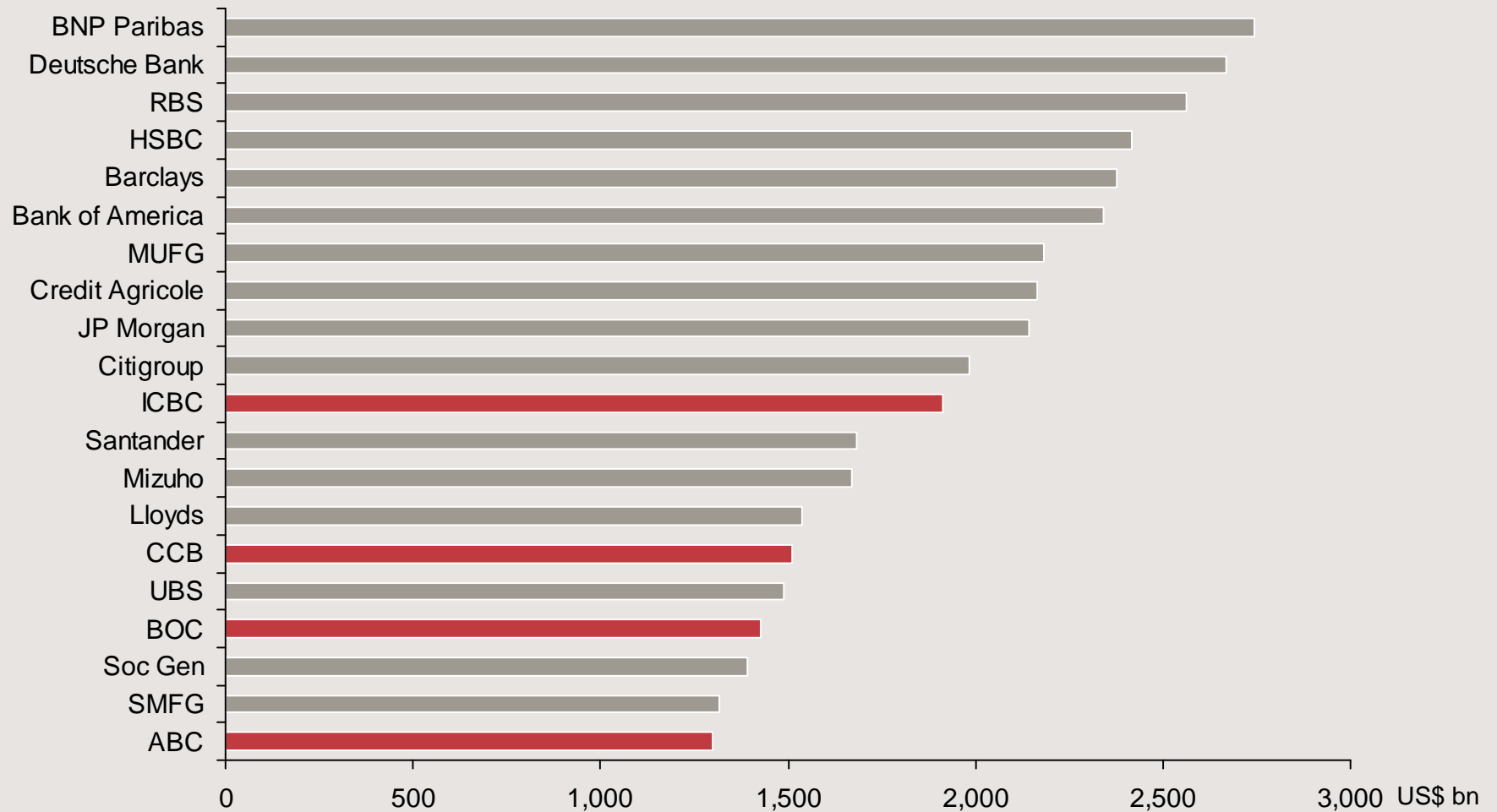
# Current Regulatory Regime & Impact of Basel III

现行规管制度及巴塞尔三的影响

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# The 20 Largest Banks in the World by Assets

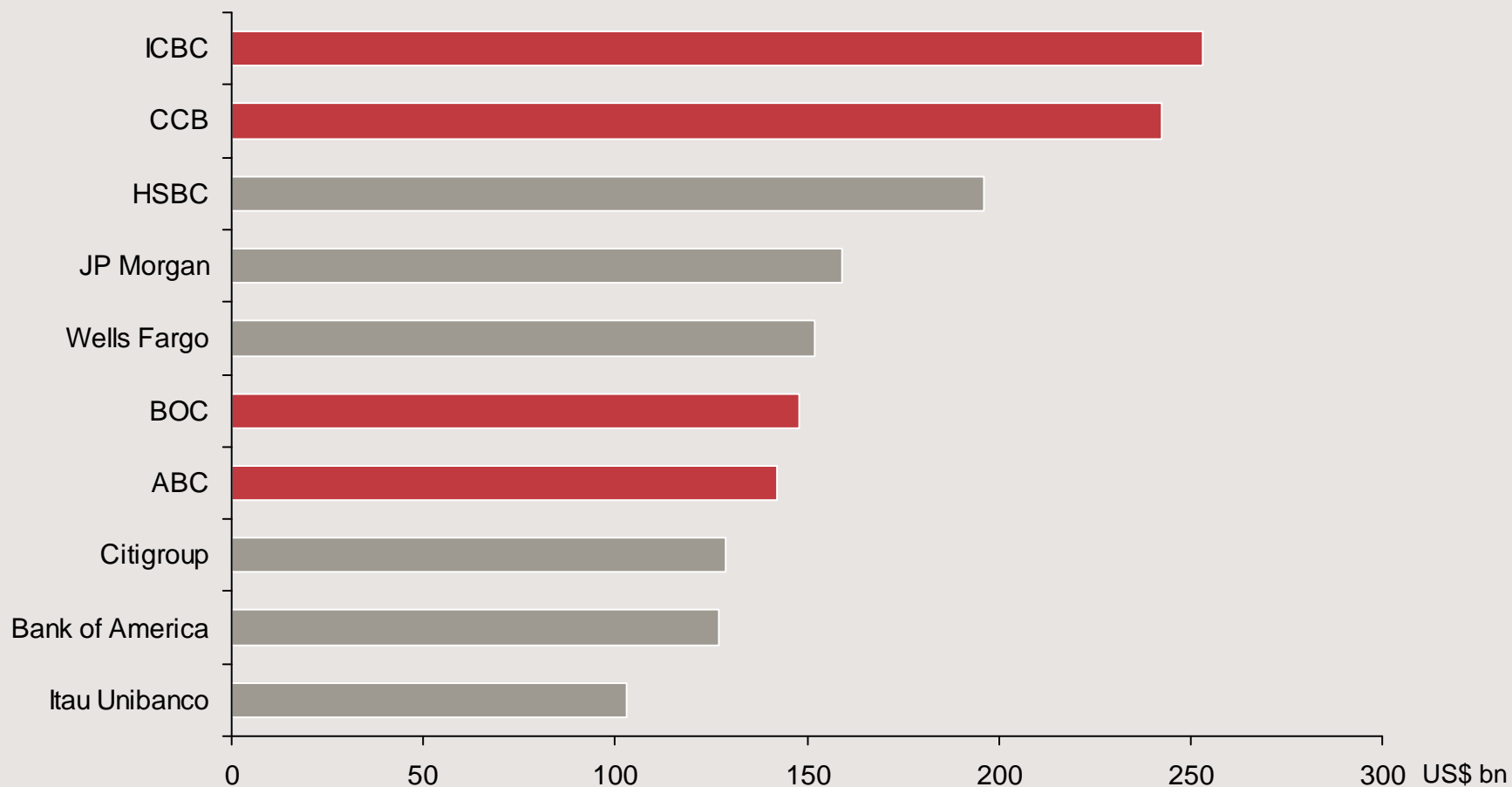
## 按资产世界二十大银行



Source: Bloomberg, 9 Nov 2010

# The 10 Largest Banks in the World by Market Capitalisation

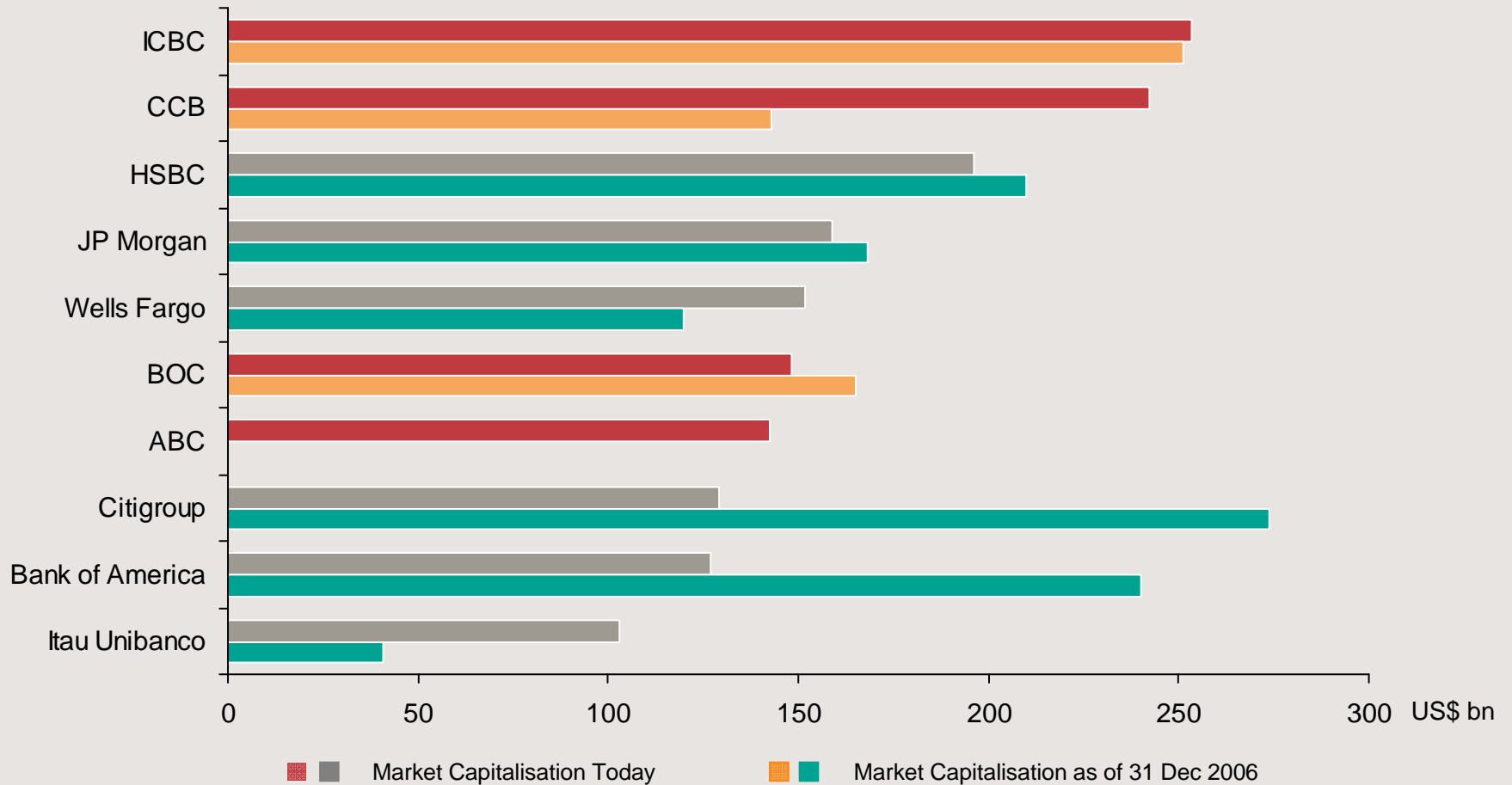
## 按市值世界十大銀行



Source: Bloomberg, 9 Nov 2010

# Top 10 Banks - Market Capitalisation in 2006 vs. Today

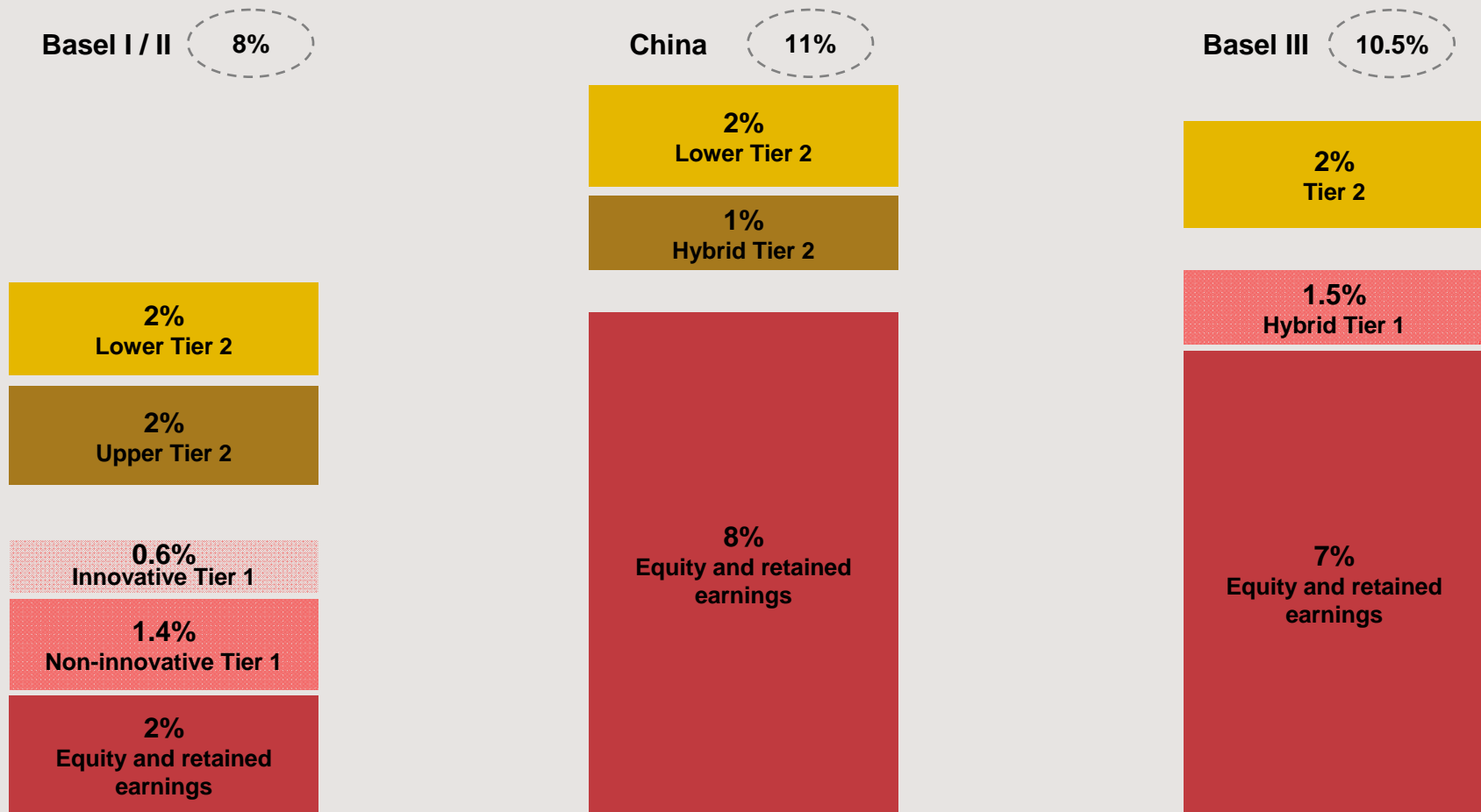
## 比较现今与2006年世界十大银行的市值



Source: Bloomberg, 9 Nov 2010

# Minimum Capital Requirements for the Largest Chinese Banks vs. the Global Standards

## 与全球标准对比中国最大银行的最低资本要求

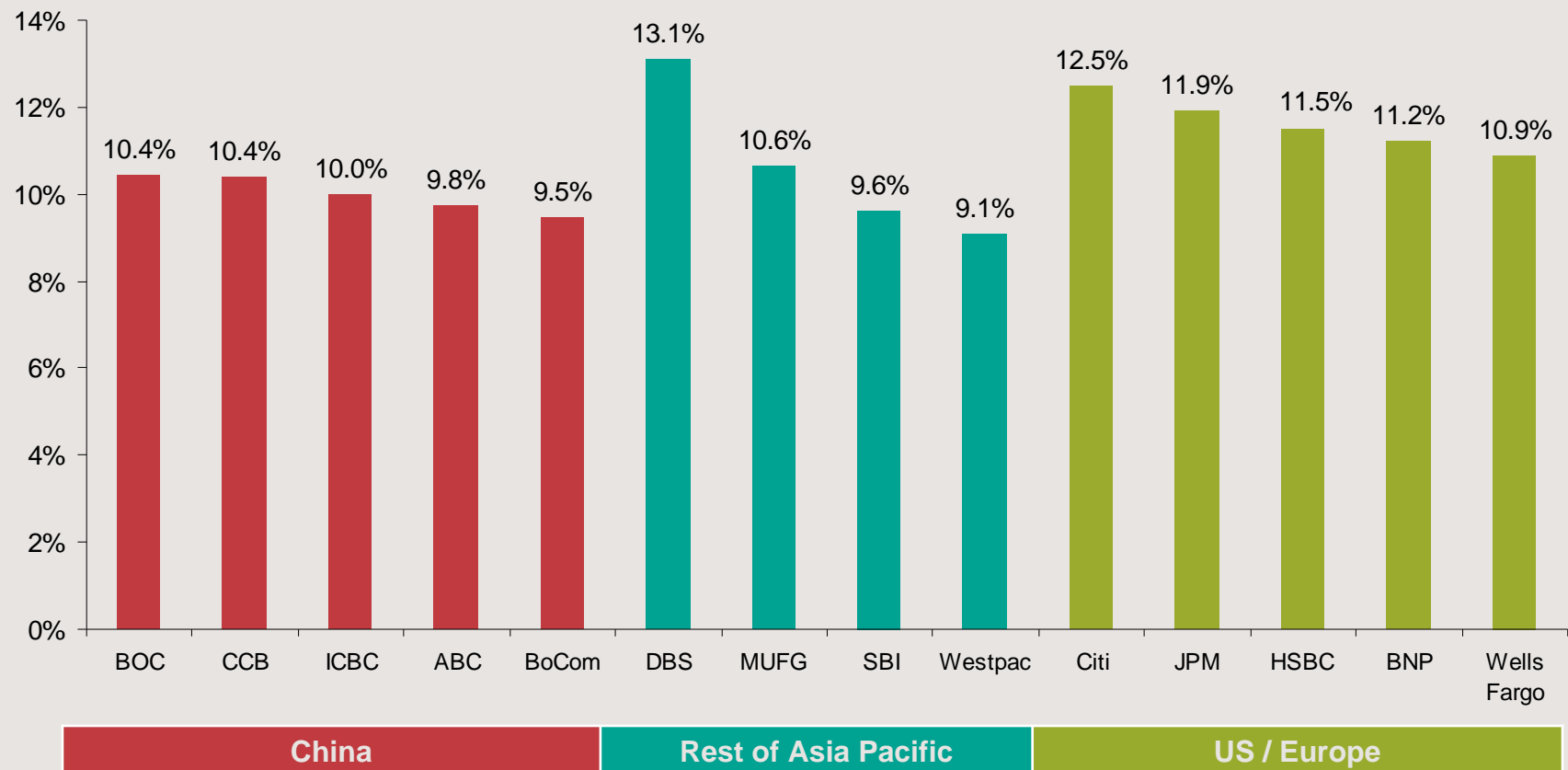


Source: BCBS, CBRC, RBS Estimates

# Tier 1 Capital Position of the Largest Chinese Banks Compared to Global Peers

## 与全球标准对比中国五大银行的一级资本比率

### Published Tier 1 Capital Ratios

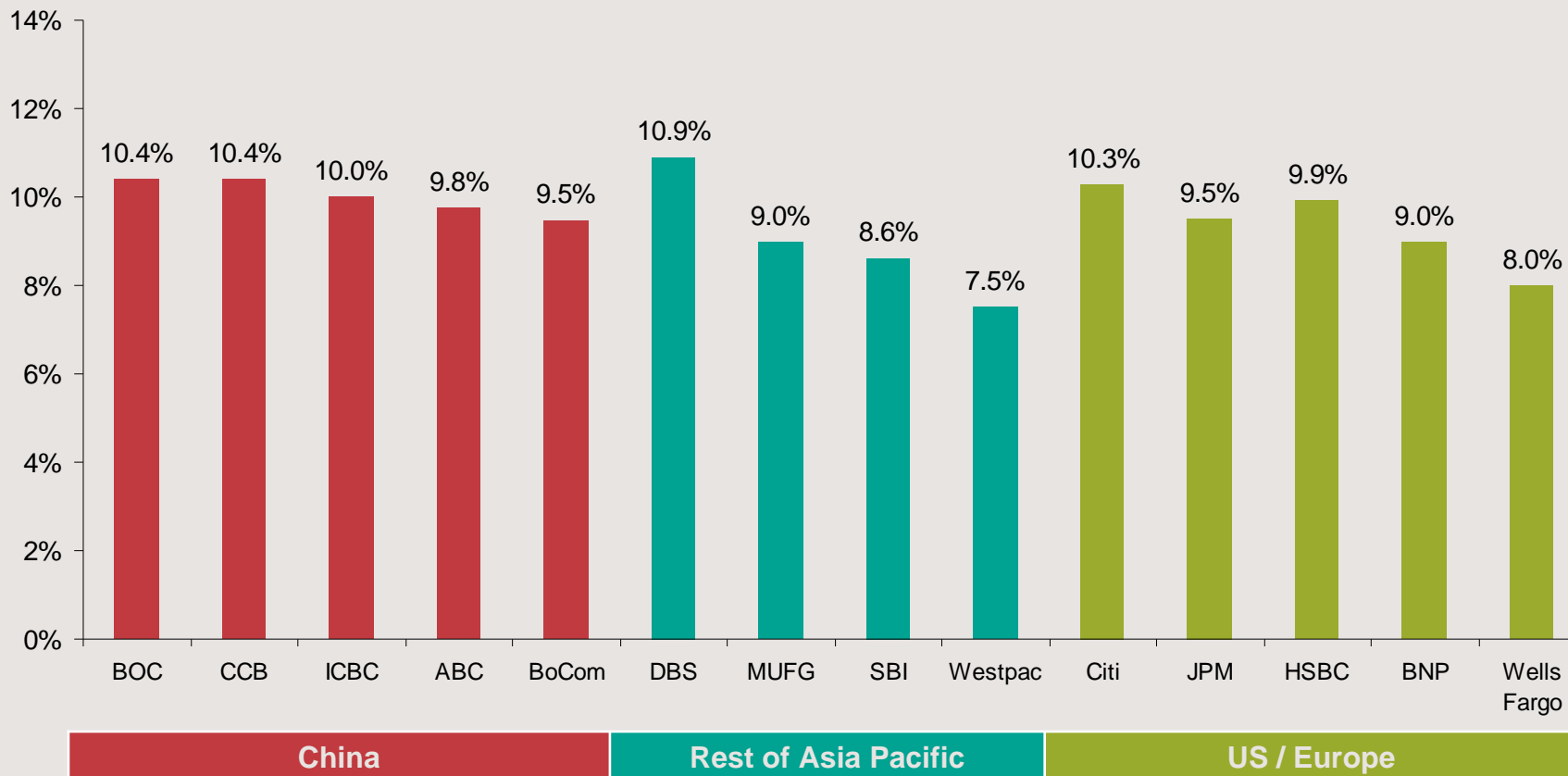


Source: Company reports, RBS estimates; Note: Chinese banks' capital ratios are adjusted for planned rights issue proceeds

# Core Tier 1 Capital Position of Largest Chinese Banks Compared to Global Peers

## 与全球标准对比中国五大银行的核心一级资本比率

### Published Core Tier 1 Capital Ratios

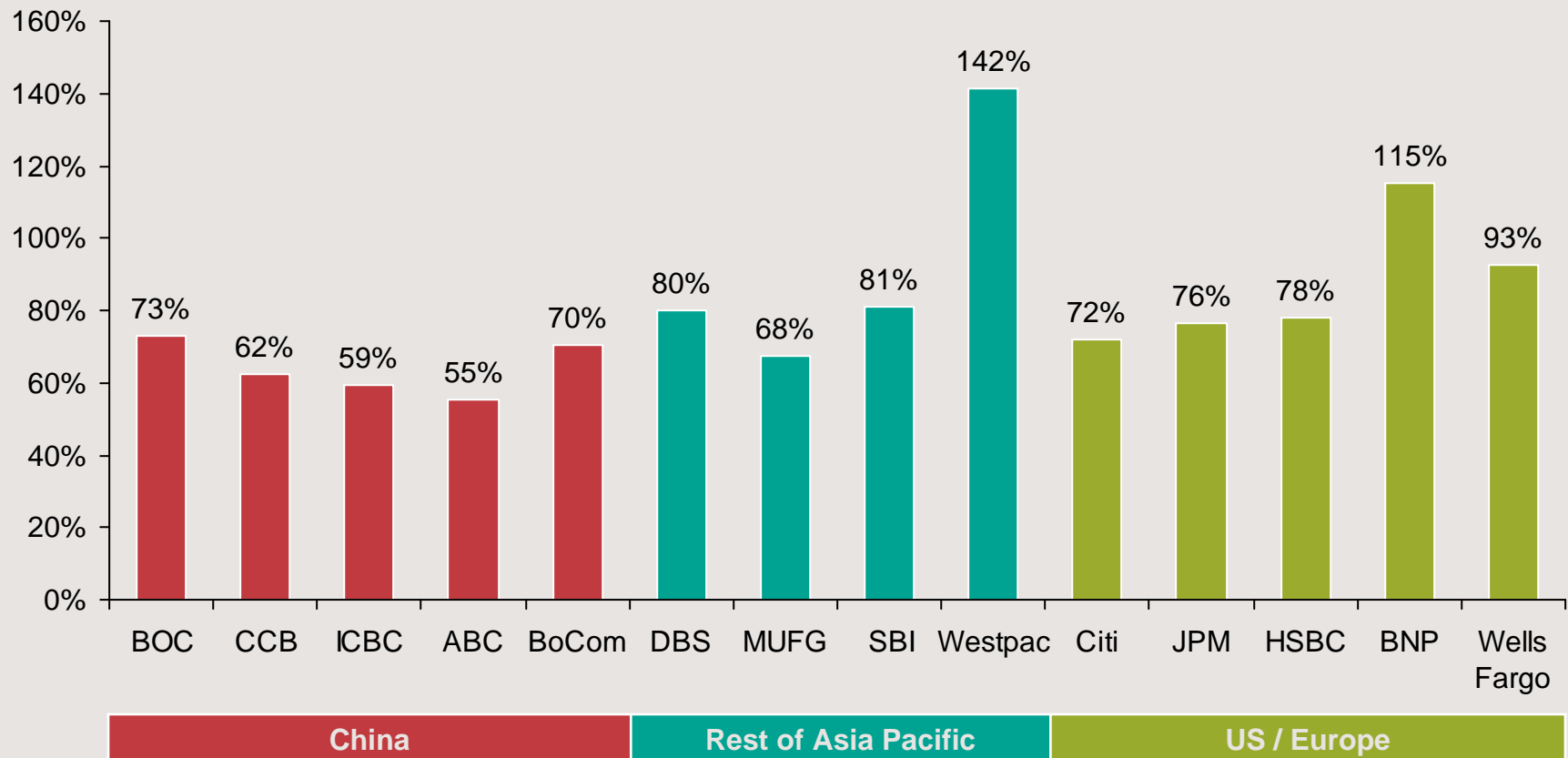


Source: Company reports, RBS estimates; Note: Chinese banks' capital ratios are adjusted for planned rights issue proceeds

# Funding Position of Largest Chinese Banks Compared to Global Peers

## 与全球标准对比中国五大银行的贷存比率

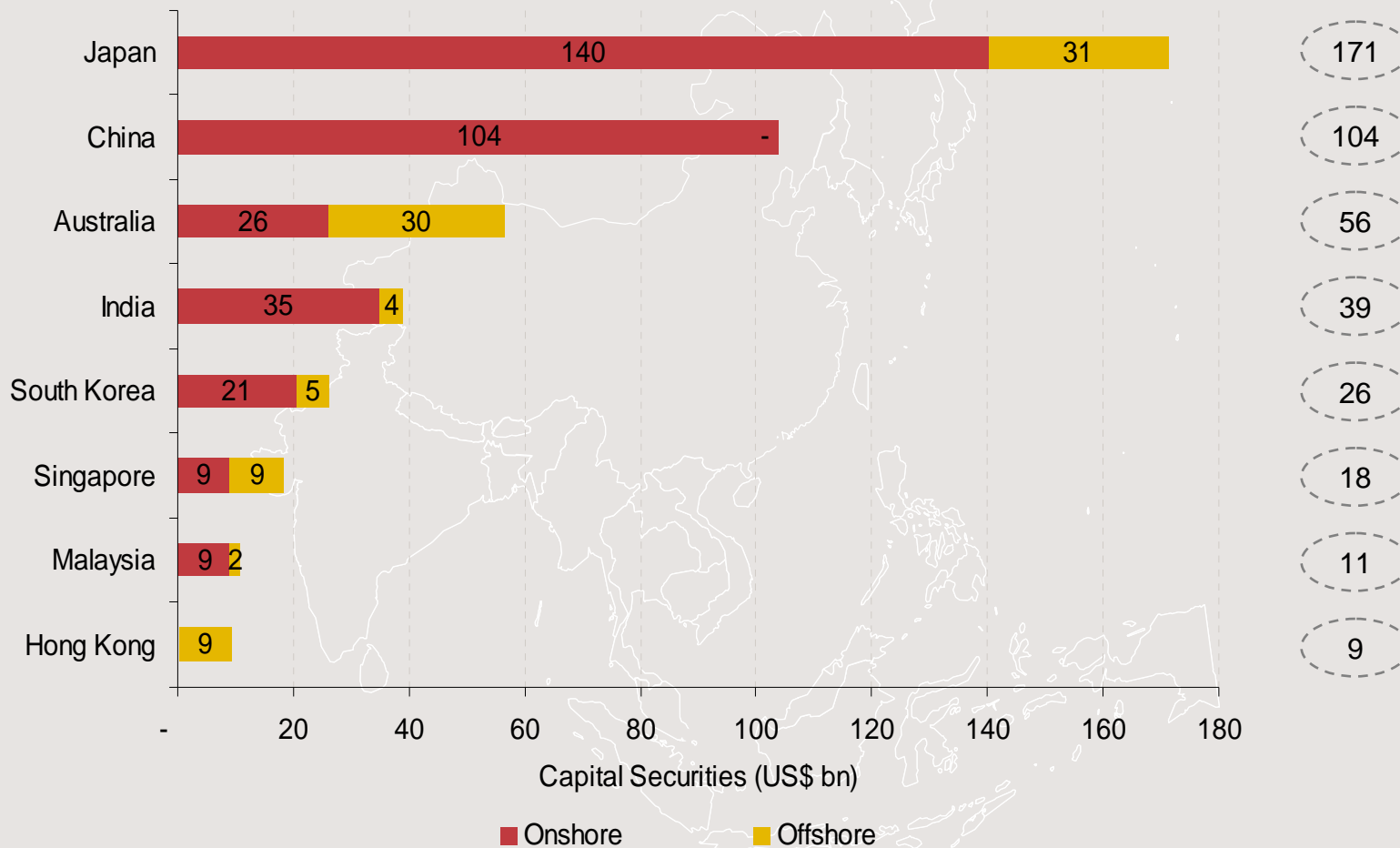
### Loan to deposit ratios



Source: Company reports, RBS estimates

# Debt Capital Securities Outstanding – Onshore vs. Offshore

## 未偿还境内与境外债务资本证券



Source: Bloomberg as on 4 October 2010

# Implementation Timeline for Regulatory Reforms

## 监管改革的实施时间表

Regulatory Agenda	Basel III Timeline	China Timeline
Common Equity Tier 1	2013	In place
Basel III Hybrid Tier 1 Instruments	2011	?
Capital Conservation Buffer	2016	2009
Countercyclical buffer	From 2013	2009
Deduction of cross holdings	2014 –'18	2009
Leverage Ratio	2013 –'18	2010
Liquidity Coverage Ratio	2015	2009
Net Stable Funding Ratio	2018	-
Elimination of Coupon Step-ups	2010	2010

Source: BCBS, RBS Bank Capital Solutions

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**Lessons from Japan and Korea**  
日本与韩国的经验借鉴

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## Bernanke believes he saved the world in 2009

伯南克认为是他拯救了世界



- Lowered interest rates
- Bailed out troubled financial institutions
- Created new facilities to “freely lend against sound collateral”
- Bought long-term debt issued by public and private institutions
- After QE I, he is now doing QE II

**Essentially, he printed a lot of dollars to buy bonds**

## But the real heroes were Chinese banks!

可是，真正的英雄是我们中国的银行！

- RMB9.6 trillion (USD1.4 trillion) of new credit in 2009
- RMB4.6 trillion (almost USD700bn) in new loans in H1
- This money was borrowed and spent, and drove economic growth



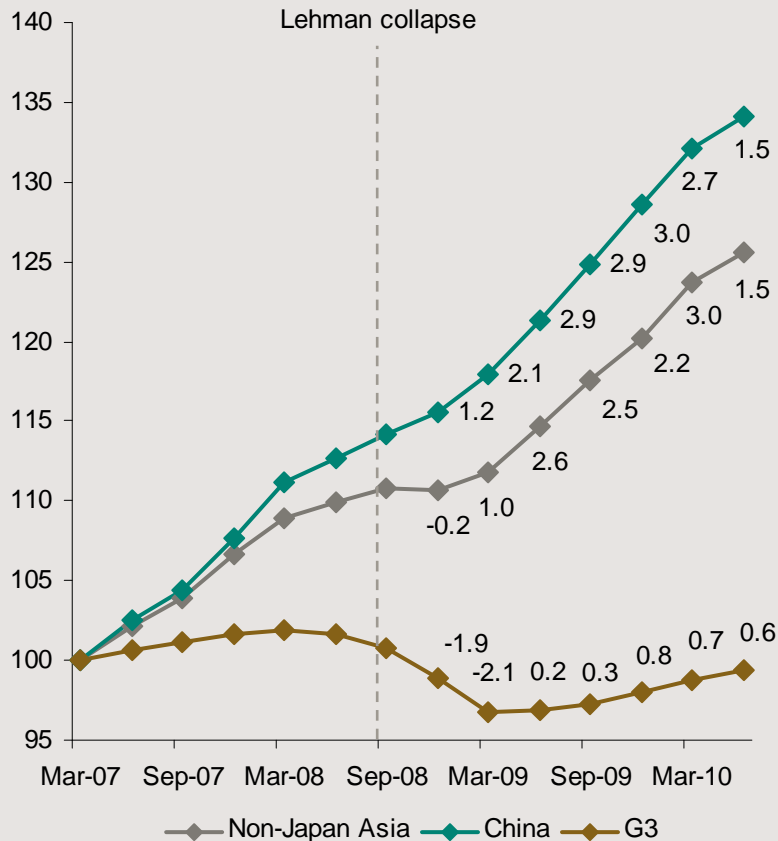
### China's loan growth versus GDP growth



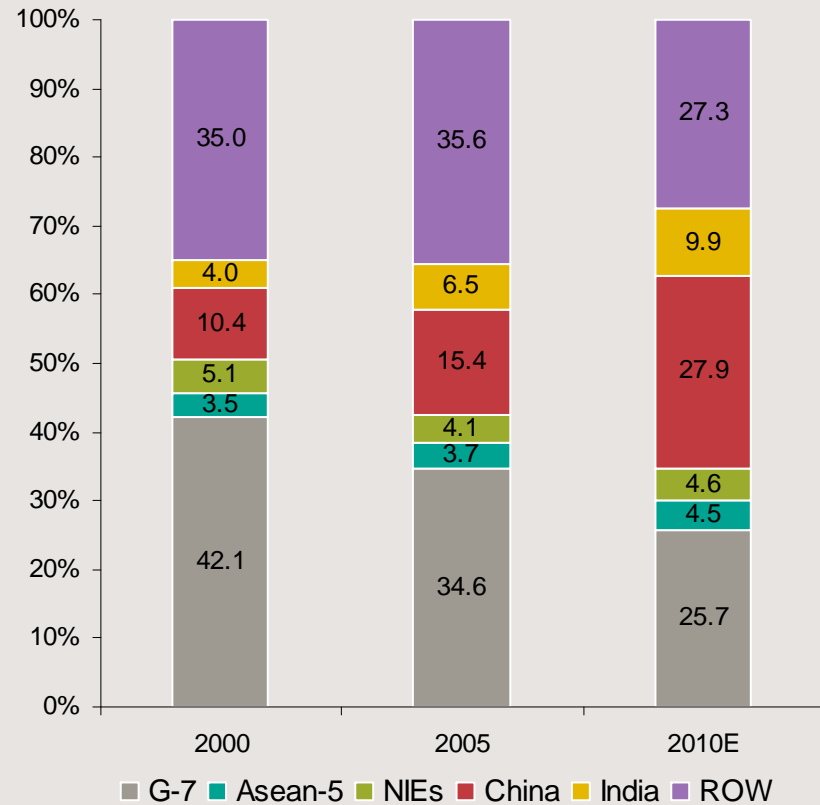
Source: CEIC, RBS

# It is China and her Asian sisters that pulled the world out of recession 是中国以及亚洲拉动了世界，走出了危机

**Real GDP growth QoQ%: China, Asia vs G3**



**Contribution to global growth (GDP on PPP basis)**



Source: CEIC, RBS

# Japanese banks were the largest in the world 20 years ago 20年前的日本银行也是世界上最大的

## World's largest banks by market cap – 1989

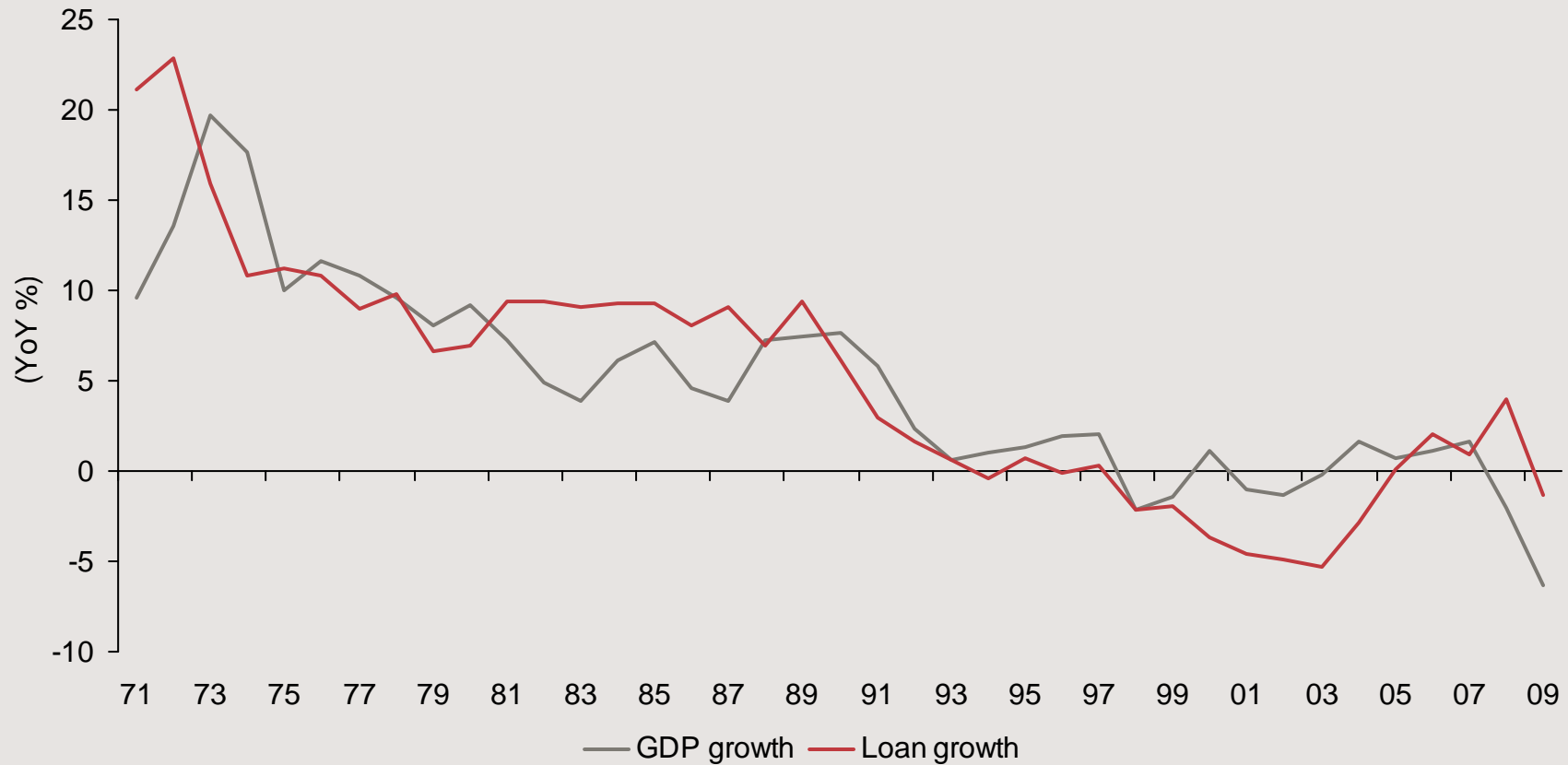
Bank	Country	Mkt Cap (US\$ bn)
Industrial Bank of Japan	Japan	104
Sumitomo Bank	Japan	72
Fuji Bank	Japan	68
Mitsubishi Bank	Japan	64
Dai-Ichi Kangyo Bank	Japan	62
Sanwa Bank	Japan	54
Nomura	Japan	47
Long-Term Credit Bank Japan	Japan	43
Tokai Bank	Japan	35
Mitsui Taiyo Kobe	Japan	35

## Total market cap of Japanese banks



Source: CEIC, RBS

## What lessons can China learn from the decline of Japanese banks? 中国可从日本银行的衰退借鉴何教训？



Source: CEIC, RBS

# And the fall and rise of Korean banks? 中国可从韩国银行的一衰一兴借鉴何教训?

Total market cap of Korean banks



Source: CEIC, RBS

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# When a real crisis struck, Japan and Korea just collapsed

## 日本和韩国都曾在危机中不堪一击

### JAPANESE BANKS

- Lent excessively in the 1980s to the property sector, because prices could never go down
- Relied on stock market gains for profits, rather than net interest income
- Never had any credit costs as all loans were collateralized with land

### THE COLLAPSE

- Triggered by BOJ monetary tightening to fight the property bubble in 1989

### KOREAN BANKS

- Lent excessively in the 1990s to the Chaebol, because they were too big to fail
- Spreads were thin, but credit costs were low since Chaebol loans were never classified as NPLs.
- Banks hated retail and SME customers

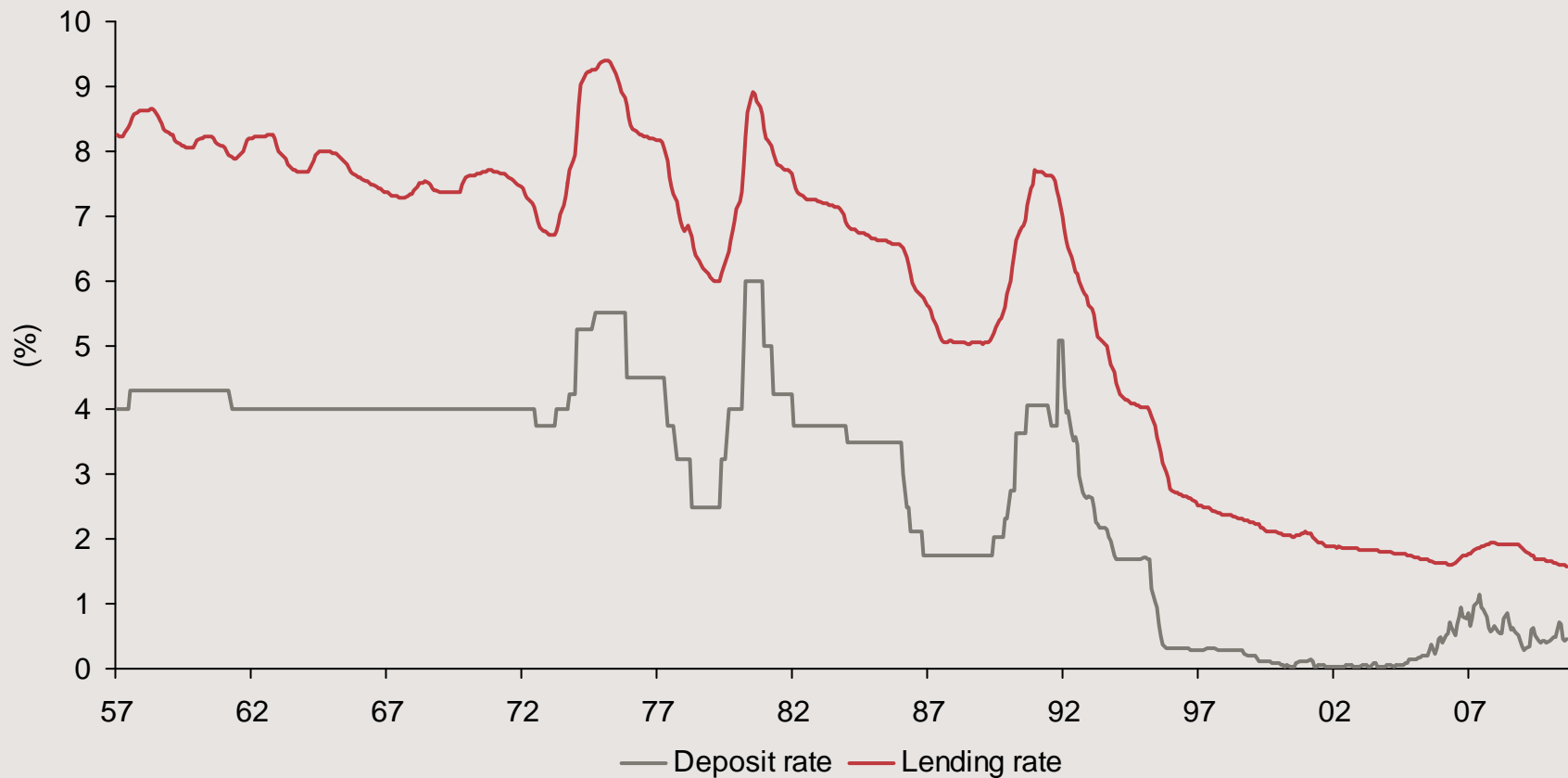
### THE COLLAPSE

- Triggered by the fall in the value of the Won, which ended the free lunch of borrowing in low-cost US dollars

# Lesson 1: Never assume the current situation will last forever

## 第1课：不能认为大好环境将永远持续

### Japanese banks' lending and deposit rates



Source: CEIC, RBS

## Lesson 2: Slower loan growth is nothing to fear

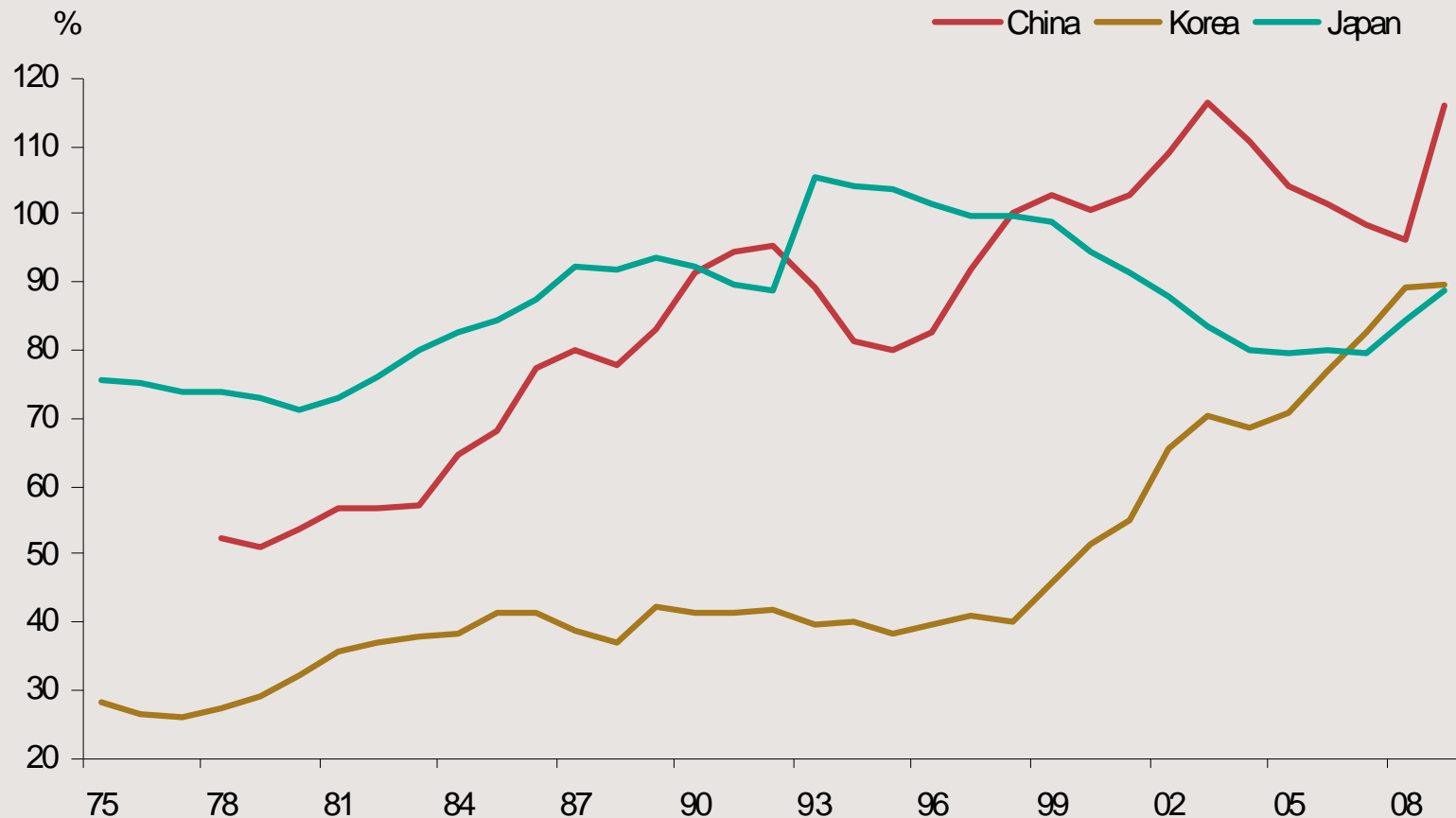
### 第2课：贷款增长放慢不是坏事

#### New loans granted by Chinese banks



Source: CEIC, RBS

## China's credit/GDP ratio is already higher than the peak of Japan 中国的信贷/GDP比率已高于日本的最高水平

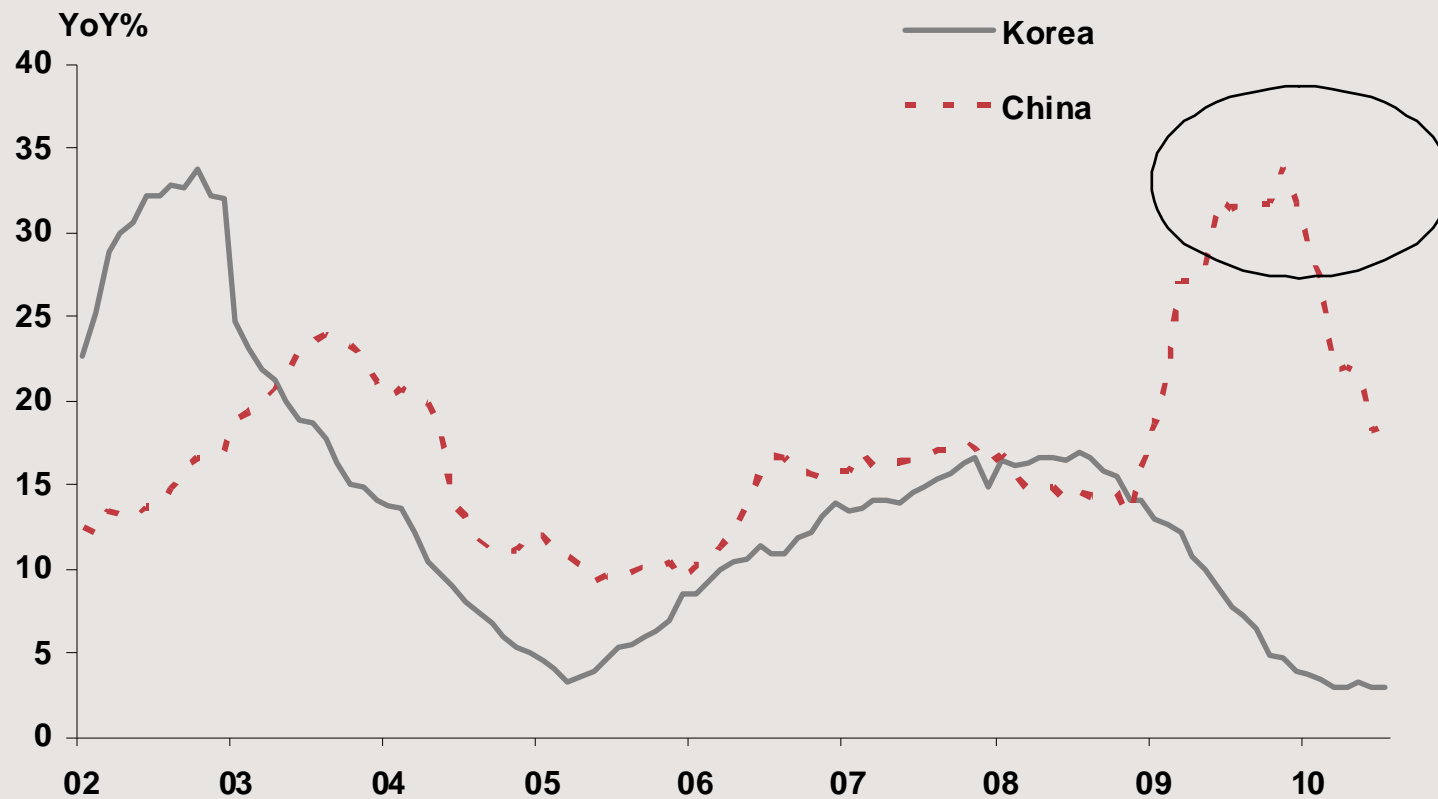


Source: CEIC, RBS

# Korean banks have been very prudent since the 2007

自2007年，韩国银行一直非常谨慎

## Loan growth YoY of Asian banks

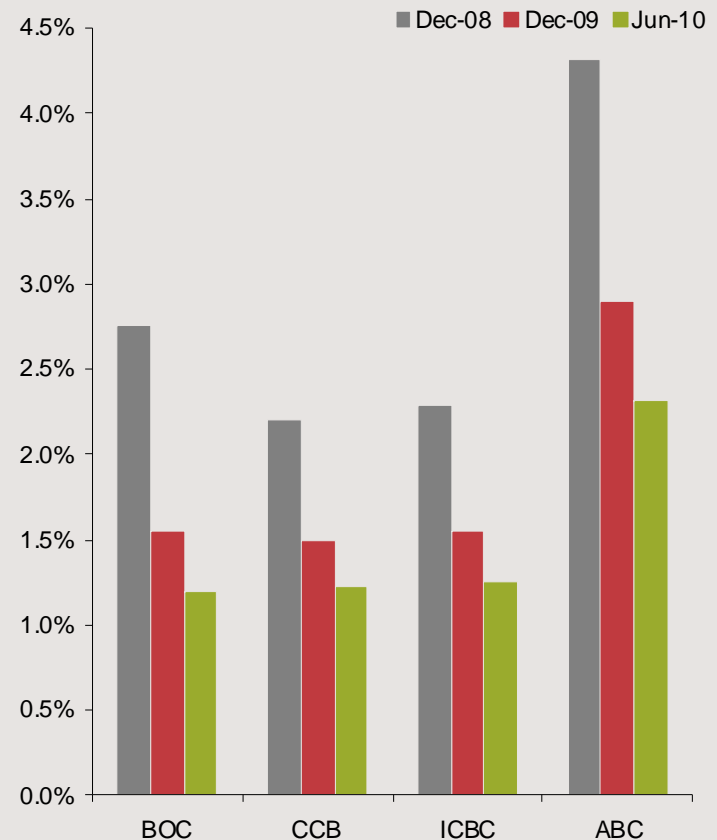


Source: CEIC, RBS

## Lesson 3: Deal with asset quality issues when NPLs are low 第3课：于不良贷款少时处理资产质量问题

- High loan growth masks NPL problems, because troubled companies can refinance and the loan denominator is growing
- The best time to deal with potential NPLs issue is when there are no NPLs.
- The Korean government is now forcing its banks to reclassify its lending and restructure their borrowers
- For Chinese banks, the issues are: loans to LGFVs, off-balance sheet lending

NPL ratios at the big Chinese banks

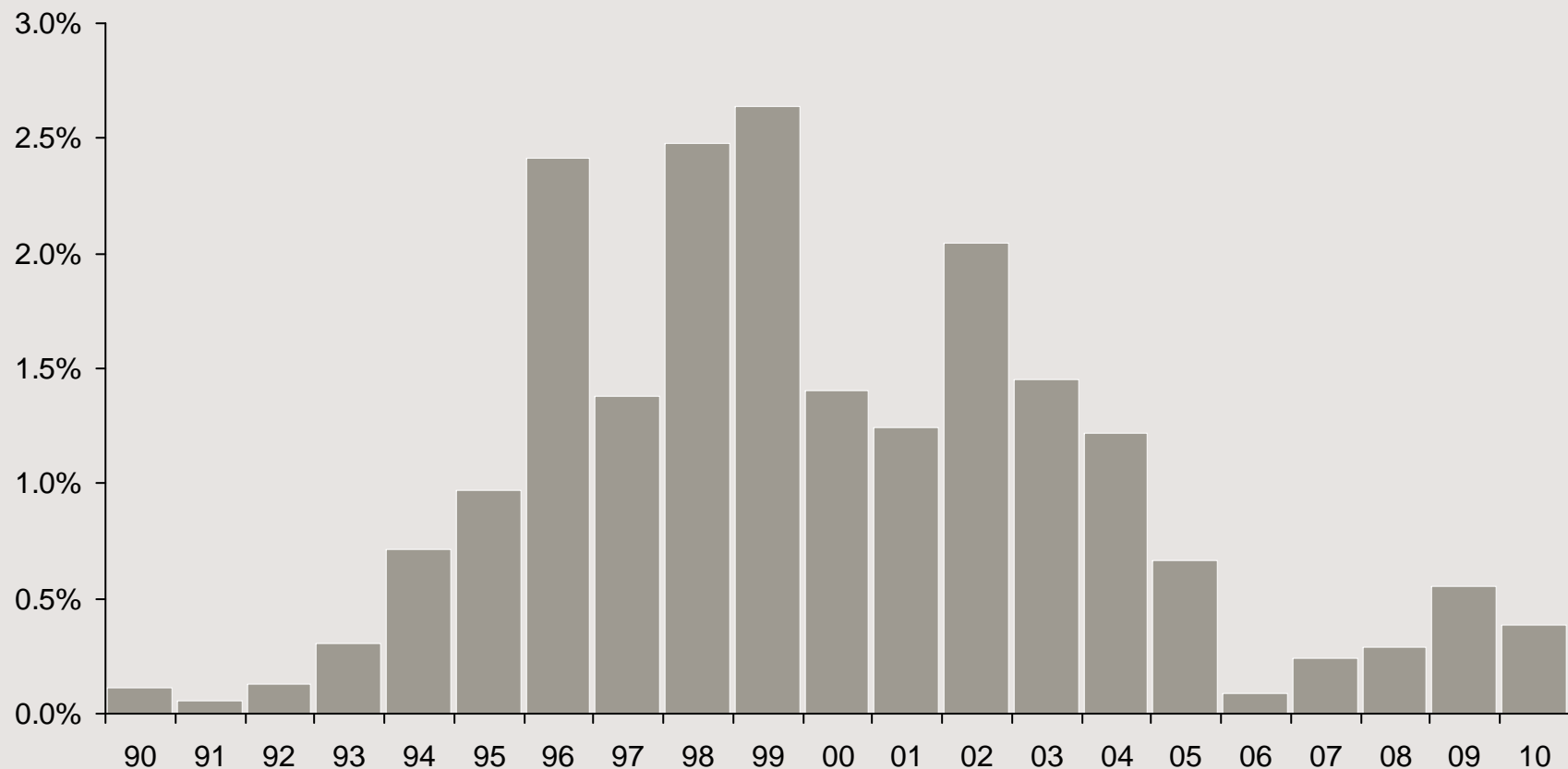


Source: Company data, RBS

# Japan only dealt with its problem loans a decade after they occurred

日本只在十年后处理问题贷款

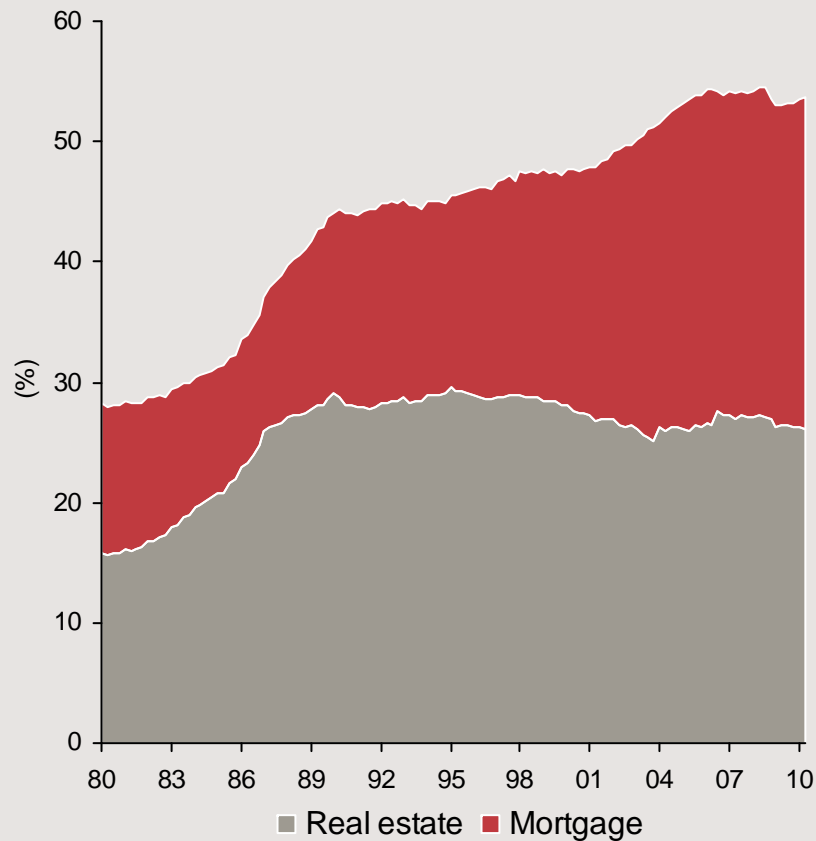
## Credit costs to loans of Japanese banks



Source: company data, RBS

## Lesson 4: Reduce property exposure, direct and indirect 第4课：减少直接和间接的房地产信贷

Japanese bank total property exposure



Property loan growth of Chinese banks



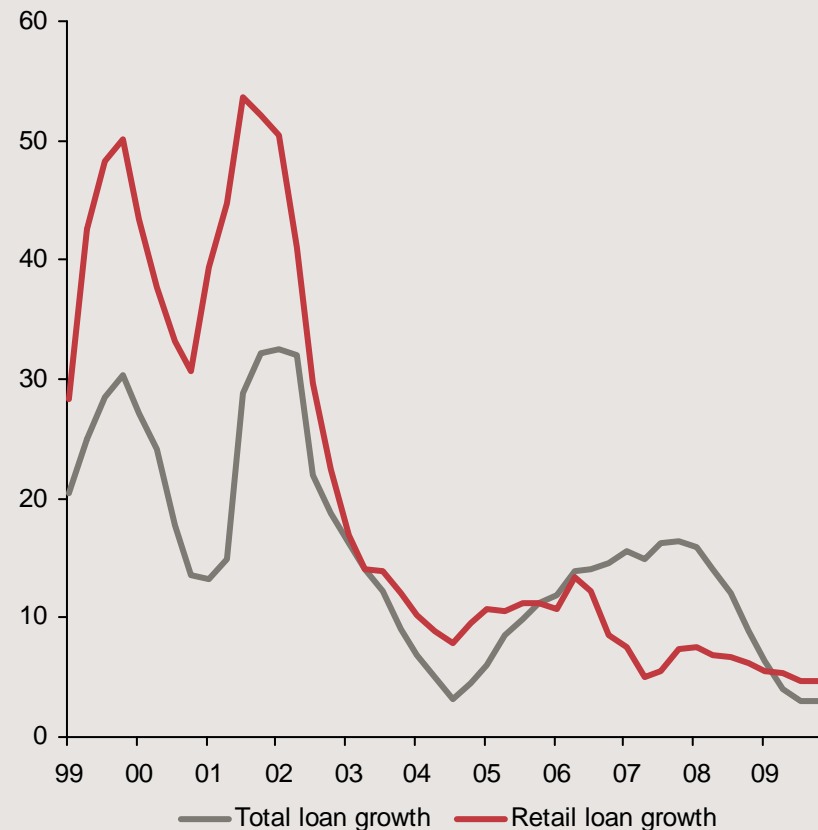
Source: CEIC, RBS

## Lesson 5: SMEs and retail customers are key

### 第5课：中小型企业 和 零售客户 是关键

- The only major Korean banks not to be nationalized after 1997 were those that focused on lending to SMEs, retail customers, and mortgages
- Since then, retail loan growth has driven total loan growth
- SMEs and retail customers are willing to pay more for loans
- Banks are forced to do more credit due diligence
- SME and retail customers allow more diversification

**Korean banks grew retail/SME loans**



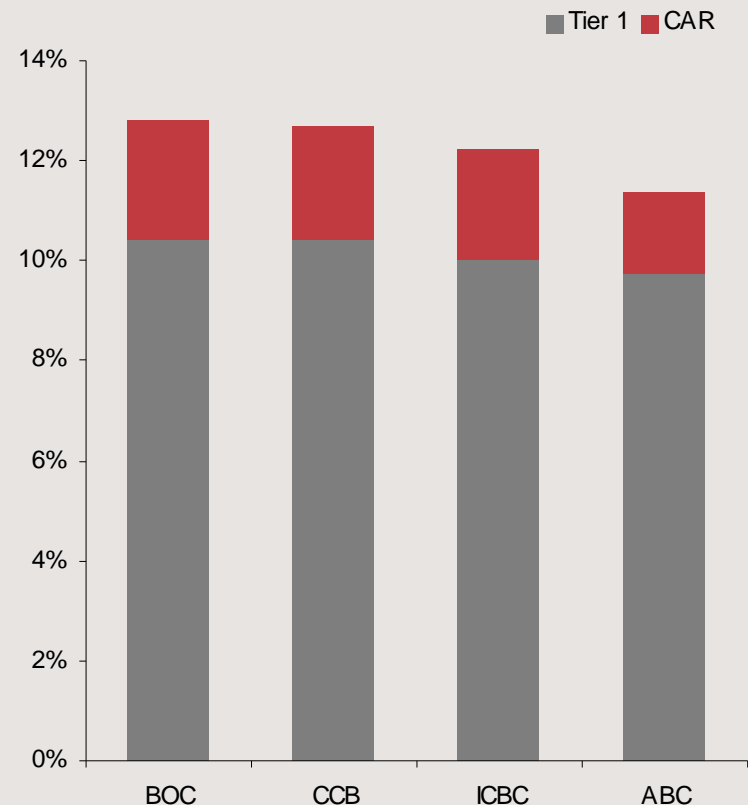
Source: CEIC, RBS

## Lesson 6: Raise capital when the market allows

### 第6课：趁市场良好时筹集资金

- The big four Chinese banks already raised or plan to raise as much as USD 80bn. With this new capital, their Tier 1 ratios will be over 10%
- It is much easier and cheaper to raise equity and sub-debt when the market is good and investors are willing to take on risk
- Capital ratios could fall even without loan growth when NPLs rise
- Basel III will require counter-cyclical buffer on banks who have high loan growth

Estimated capital ratios post equity raising



Source: Company data, RBS

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## Lesson 7: Do not hesitate to deal with problems when they occur

### 第7课：问题发生时必需马上处理

#### What Korea did in the first year of crisis

- Fired 31% of all bankers in 1998
- Replaced management in 12 banks
- Nationalized/merged 13 banks
- Brought disclosure up to world standards
- Sold W39 trillion in NPLs to KAMCO
- Supported banks with redeemable preferred shares
- Sold two major bank to foreigners
- Forced the Chaebol to restructure

#### What Japan did in the first decade of crisis

- Reduced headcount by 6% in six years
- Left the old management in charge
- Had banks do a “self-assessment” of NPLs
- Allowed the banks to keep NPLs on their books
- Reduced banks from 144 in 1991 to 139 today
- Sold no banks to foreigners
- Put no pressure on keiretsu to restructure
- Came up with Y60 trillion to recapitalize banks

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## Lesson 8: Banks do not create strong economies, they support strong economies

### 第8课：经济强盛不能全靠银行，银行支持经济发展

- The best time to strengthen the banking industry is during the good times, not after a crisis has occurred.
  - Earnings are high to absorb additional loan loss reserves
  - Capital market is hot – easier to raise equity and sub-debt
- The best case scenario is that China allows the banks to slow down their lending, focus on asset quality and build up their capital.
- Shift focus from corporate lending to more profitable SME and retail lending

Source: CEIC, RBS

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