

INDUSTRY OVERVIEW

This section contains information and statistics on the industry in which our Bank operates. We have extracted and derived such information and statistics, in part, from statistics relating to our Group prepared in accordance with IFRS, and, in part, from various official or publicly available sources where such information and statistics were derived from data prepared in accordance with PRC GAAP or other applicable GAAP or accounting standards that may differ from IFRS in certain significant respects.

We believe that the sources from which this information and statistics are taken are appropriate sources for such information and statistics and we have taken reasonable care in extracting and reproducing such information and statistics. We have no reason to believe that such information and statistics are false or misleading or that any fact has been omitted that would render such information and statistics false or misleading. The information and statistics have not been independently verified by us, the Joint Sponsors, the Underwriters or any other party involved in the Global Offering and no representation is given as to their accuracy. Accordingly, such information and statistics should not be unduly relied on.

OVERVIEW

China's Economy

China's economy has grown significantly over the past three decades as a result of the Chinese government's extensive economic reforms. These reforms originally focused on transforming China from a centrally planned economy to a more market-based economy. More recently, particularly following China's accession to the WTO in 2001, such economic reforms have also aimed, among other things, at enhancing the competitiveness of Chinese enterprises. As a consequence of the various reforms mentioned above, China's nominal GDP grew at a CAGR of 13.4% from RMB31,405 billion to RMB51,947 billion between 2008 and 2012 according to the NBSC, notwithstanding the impact of the global economic recession. The table below sets out China's GDP, fixed asset investments and total import and export value, as well as the respective CAGRs, for each year from 2008 to 2012.

	Year ended 31 December					CAGR (2008-2012)
	2008	2009	2010	2011	2012	
Nominal GDP (in billions of RMB)	31,405	34,090	40,151	47,310	51,947	13.4%
Per capita GDP (in RMB)	23,708	25,608	30,015	35,198	38,420	12.8%
Fixed asset investments (in billions of RMB) . . .	17,283	22,460	25,168	31,149	37,469	21.3%
Total import and export value (in billions of USD)	2,563	2,208	2,974	3,642	3,867	10.8%

Source: NBSC

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The rapid growth of China's economy has driven the expansion of the banking industry. From 2008 to 2012, the total RMB-denominated loans and deposits of China's banking institutions increased at CAGRs of 20.0% and 18.4%, respectively. On a year-on-year basis, the total amount of RMB-denominated loans increased by 31.7%, 19.9%, 14.3%, and 15.0%, respectively, from 2009 to 2012. Although the growth of RMB-denominated loans has slowed down over the same period, the total amount of RMB-denominated loans kept growing at a relatively fast rate of more than 14%, which demonstrated the significant financing demand in China and the strength of the PRC economy. The table below sets out the total RMB-denominated loans and deposits and the total foreign currency-denominated loans and deposits, in each case, from 2008 to 2012, for banking institutions in China.

	Year ended 31 December					CAGR (2008-2012)
	2008	2009	2010	2011	2012	
Total RMB-denominated loans (in billions of RMB)	30,347	39,968	47,920	54,794	62,991	20.0%
Total RMB-denominated deposits (in billions of RMB)	46,620	59,774	71,823	80,937	91,737	18.4%
Total foreign currency-denominated loans (in billions of US\$)	244	380	453	539	684	29.4%
Total foreign currency-denominated deposits (in billions of US\$)	179	209	229	275	406	22.7%

Source: PBOC

Economy of Heilongjiang Province

Heilongjiang Province is the northernmost province in Northeast China and adjoins Russia. Benefiting from political support and its geographical environment, Heilongjiang Province has become an important commodity grain base within China. In 2012, its annual grain output ranked first in China, making up one tenth of China's total grain output. Heilongjiang Province is also rich in timber and mineral resources. After decades of development and reform, Heilongjiang Province has gradually established an industrial system which is based around heavy industry and large enterprises, with a particular focus on the petrochemical, food, machinery, coal and forest industries.

The development strategy of revitalising the old industrial bases in Northeast China since 2003, the stable income contribution from agriculture and the strengthened export-oriented economy have resulted in an improved infrastructure and an accelerated economic growth in Heilongjiang Province in recent years. From 2008 to 2012, Heilongjiang Province's nominal GDP grew at a CAGR of 13.3%, which is in line with the rapid growth of China's economy. The table below sets out Heilongjiang Province's GDP, fixed asset investments and total import and export value as well as the respective CAGRs from 2008 to 2012.

	Year ended 31 December					CAGR (2008-2012)
	2008	2009	2010	2011	2012	
Nominal GDP (in billions of RMB)	831	859	1,037	1,258	1,369	13.3%
GDP per capita (in RMB)	21,740	22,447	27,076	32,819	35,711	13.2%
Fixed asset investments (in billions of RMB) ...	366	503	681	748	969	27.6%
Total import and export value (in billions of USD)	23	16	26	39	38	12.9%

Source: NBSC

Alongside the economic development of the region, the banking industry in Heilongjiang Province has also experienced rapid growth. According to the statistics compiled by the Statistics Bureau of

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Heilongjiang Province, as of 31 December 2012, the total RMB-denominated deposits of banking institutions in Heilongjiang Province reached RMB1,632.66 billion, representing an increase of 14.0% compared to the beginning of 2012, whilst total RMB-denominated loans in Heilongjiang Province reached RMB990.67 billion, representing an increase of 15.9% compared to the beginning of 2012.

The table below sets out the total RMB-denominated loans and deposits and the total foreign currency-denominated loans and deposits, and the respective CAGRs of banking institutions in Heilongjiang Province from 2008 to 2012.

	Year ended 31 December					CAGR (2008-2012)
	2008	2009	2010	2011	2012	
Total RMB-denominated loans (in billions of RMB)	453.26	598.83	723.05	854.87	990.67	21.6%
Total RMB-denominated deposits (in billions of RMB)	899.38	1,102.28	1,283.57	1,432.84	1,632.66	16.1%
Total foreign currency-denominated loans (in millions of US\$)	1,230	1,380	1,340	1,400	3,410	29.0%
Total foreign currency-denominated deposits (in millions of US\$)	900	2,300	2,420	3,370	5,620	58.1%

Source: 2008 – 2012 Heilongjiang Statistics Year Book and PBOC Harbin Central Sub-branch

CURRENT COMPETITIVE LANDSCAPE OF THE PRC BANKING INDUSTRY AND OUR ADVANTAGES

China's banking institutions are generally categorised into Large Commercial Banks, Nationwide Joint-stock Commercial Banks, city commercial banks, rural financial institutions, foreign financial institutions and other banking institutions. The table below sets out the number of institutions, total assets, shareholders' equity and net profit of the different categories of banking institutions in China as of 31 December 2012.

China	As of 31 December 2012						
	Number of legal entity institutions	Total assets		Shareholders' equity		Net profit	
		Total amount	Market share	Total amount	Market share	Total amount	Market share
(in billions of RMB, except number of institutions and percentages)							
Large Commercial Banks	5	60,040	44.94%	3,952	45.58%	755	49.92%
Nationwide Joint-stock Commercial Banks	12	23,527	17.61%	1,314	15.16%	253	16.71%
City commercial banks	144	12,347	9.24%	808	9.31%	137	9.05%
Rural financial institutions ⁽¹⁾	2,411	15,512	11.61%	996	11.49%	161	10.64%
Foreign financial institutions ⁽²⁾	412	2,380	1.78%	256	2.95%	16	1.08%
Other banking institutions ⁽³⁾	1,133	19,816	14.82%	1,345	15.51%	190	12.59%
Total	3,747	133,622	100.00%	8,671	100.00%	1,512	100.00%

Source: CBRC 2012 Annual Report

Notes:

- (1) Consist of rural credit cooperatives, rural commercial banks and rural cooperative banks.
- (2) Consist of foreign bank branches, foreign-owned banks, Sino-foreign joint-ventured banks and foreign-owned finance companies and their branches and subsidiaries.
- (3) Consist of policy banks, China Development Bank, the Postal Savings Bank of China and other non-bank financial institutions, including banking asset management companies, finance companies affiliated to corporate enterprises, consumer finance companies, trust companies, financial leasing companies, money brokerage firms, auto financing companies, Village and Township Banks, lending companies and rural mutual cooperatives.

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The table below sets out, as of 31 December 2012, certain information relating to the total assets, total shareholders' equity, and net profit of different categories of banking institutions in Heilongjiang Province and that of our Bank.

<u>Heilongjiang Province</u>	<u>As of 31 December 2012</u>						
	<u>Number of institutions⁽¹⁾</u>	<u>Total assets</u>		<u>Shareholders' equity</u>		<u>Net profit</u>	
		<u>Total amount</u>	<u>Market share</u>	<u>Total amount</u>	<u>Market share</u>	<u>Total amount</u>	<u>Market share</u>
(in billions of RMB, except number of institutions and percentages)							
Large Commercial Banks	5	937	39.87%	12	17.14%	8	30.77%
Nationwide Joint-stock Commercial Banks	6	174	7.40%	3	4.29%	2	7.69%
City commercial banks ⁽²⁾	6	473	20.13%	26	37.14%	5	19.23%
Rural financial institutions	89	240	10.21%	14	20.00%	0.3	1.15%
Foreign financial institutions	6	4	0.17%	1	1.43%	0.01	0.04%
Other banking institutions	40	522	22.21%	14	20.00%	10.69	41.12%
Total	152	2,350	100.00%	70	100.00%	26	100.00%

Source: CBRC Heilongjiang Bureau

Notes:

- (1) Including institutions incorporated or have branch established in Heilongjiang Province.
- (2) Our Bank is a city commercial bank, being one of six city commercial banks in Heilongjiang Province.

As of 31 December 2012, our Bank's total assets, total shareholders' equity and net profit were approximately RMB270.1 billion, RMB16.9 billion and RMB2.9 billion, respectively. Based on a confirmation letter issued by the CBRC Heilongjiang Bureau in July 2013, we were the second largest commercial bank in Heilongjiang Province, and the largest commercial bank in Harbin in terms of total assets as of 31 December 2012 and net profit for the year ended 31 December 2012.

We were ranked 4th among the city commercial banks in the PRC according to the "2013 Research Report on Asian Bank Competitiveness Rankings" released by the 21st Century Business Herald, representing an advancement of five places as compared with 2012. The ranking is based on statistics of eight aspects relating to a bank's capabilities to enhance capital value for its shareholders, which include return on capital, market share, asset quality and capital adequacy ratio¹. We were ranked 33rd in terms of total assets among the "Top 50 Banks in China" published by Standard & Poor's in 2012. We were ranked 9th among the city commercial banks with assets scale of over RMB200 billion as published by The Banker, a PRC-based magazine in 2013, and the city commercial banks are ranked by several indicators of financial performance, including total assets, risk profile, capital structure, profitability and liquidity ratio. Our Bank was ranked 313th in the "Top 1000 World Banks 2013" recently announced by The Banker, a UK-based magazine, in terms of total tier 1 capital², representing an advancement of 85 places as compared with our ranking in the same list of the previous year. According to the list, 96 banks in the PRC ranked among the "Top 1000 World Banks 2013". Among such banks on the list, we were ranked 27th among banks in the PRC, 7th among city commercial banks in the PRC, and first among city commercial banks in Northeast China.

¹ A bank's asset scale, liquidity and efficiency indicators, deposit structure and branch network are also taken into consideration in the calculation.

² The banks are also assessed with other secondary indicators, namely assets, capital asset ratio, pre-tax profits, profit on capital, return on assets, capital adequacy ratio, NPL to total loans, loans to assets, RWA to assets and cost to income.

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INDUSTRY TRENDS

Enhanced Industry Fundamentals

Since 2003, the transformation of State-owned commercial banks into joint-stock commercial banks has had a profound effect on the reform and development of the banking industry in China. Since then, the China banking sector has witnessed significant improvement in the areas of corporate governance, risk management, capital base, profitability, branding and market recognition. From 2008 to 2012, according to CBRC 2012 Annual Report, the total assets of banking institutions in China increased by RMB70,471 billion, representing a CAGR of 20.6%, whilst total shareholders' equity increased by RMB4,881 billion, representing a CAGR of 23.0%. The asset quality of commercial banks in China also improved significantly. During the same period, non-performing loans of the banking institutions in China decreased from RMB564 billion to RMB493 billion and their non-performing loan ratio decreased from 2.42% to 0.95%.

Enhanced Regulation and Supervision

China's banking regulators have established, and continue to enhance, a prudent regulatory framework and, at the same time, continue to push forward China's financial reforms in a number of areas such as corporate governance, internal control, compliance and risk management. Furthermore, regulations have been implemented to strengthen information disclosure requirements and coordination and cooperation with domestic and foreign regulators.

Following the global financial crisis in 2008, the CBRC has reinforced its policy objectives towards prudential supervision and counter-cyclical regulation.

Prudent supervision: the CBRC has established rules and regulations to guide commercial banks to further improve their risk management systems and establish prudent measures to prevent excessive exposure to high-risk markets and industries. These regulatory measures cover a wide range of potential risks including credit, market, operational and liquidity risks.

As part of its prudent supervision, the CBRC has established a series of measures and guidelines in accordance with the development of the Basel Accords to strengthen commercial banks' capital management capabilities. These measures and guidelines relate to, among other things, capital adequacy ratio disclosure, capital measurement and risk exposure calculations.

Counter-cyclical regulation: the CBRC has also established guidelines aimed at encouraging commercial banks to better address the borrowing needs generated by the growing economy whilst also effectively managing potential risks. Specific measures include encouraging the extension of merger and acquisition loans and specialised management of lending to small businesses, broadening industry scope for project financing and promoting innovative credit guarantee and consumer loan insurance mechanisms.

Enhanced regulations on certain industries and customers: the CBRC has issued a series of regulations relating to the real estate industry and local government financing vehicles, which have restricted the amount of loans provided to such entities by PRC commercial banks, and have imposed a requirement on PRC commercial banks to enhance risk management with regard to such entities.

Improvement of corporate governance: the CBRC has encouraged banks to establish corporate governance structures, such as a board of directors comprising independent directors, an audit committee, a remuneration and nomination committee and other board committees, as well as a supervisory board.

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Moreover, the CBRC also requires PRC banking institutions to establish an independent internal audit function which has clear policies and procedures.

See “Supervision and Regulation – PRC Banking Supervision and Regulation”.

Increasing Role of City Commercial Banks in China’s Banking Industry

City commercial banks are banks with branches at the municipality level or above, and were created under the PRC Company Law and the PRC Commercial Banking Law with the approval of the CBRC. The predecessors of city commercial banks were urban credit cooperatives. In 1995, the State Council decided to restructure urban credit cooperatives into city cooperative banks, which since 1997 were referred to as city commercial banks. According to CBRC 2012 Annual Report, as of 31 December 2012, there were 144 city commercial banks in China. City commercial banks have played an active role in maintaining regional financial stability, promoting market competition, facilitating the development of financial services and easing funding pressures for SMEs.

As opposed to Large Commercial Banks and Nationwide Joint-stock Commercial Banks, city commercial banks are generally focused on providing banking services to institutions and individuals in certain specified geographic areas. From 2004 to 2011, city commercial banks were, subject to CBRC approval, also permitted to expand and establish cross-regional branches operating in other provinces. However, in 2012, the CBRC temporarily suspended the approval of new applications from banks seeking to expand in this way. As of 31 December 2012, our Bank had five branches outside Heilongjiang Province.

Leveraging their understanding of local markets and relationships with local customers, city commercial banks are generally well-positioned to capture opportunities and trends in local areas. From 2008 to 2012, the key financial indicators and performance of city commercial banks have continued to improve and the rapid development of city commercial banks has been a key reason contributing to the overall growth of China’s banking industry. According to the CBRC, the total assets of city commercial banks as a percentage of the total assets of the banking industry in China, increased from 6.5%, or RMB4.1 trillion, as of 31 December 2008, to 9.2%, or RMB12.3 trillion, as of 31 December 2012, representing a CAGR of 35.1%, which is higher than the corresponding CAGR of all other PRC banking institutions. During the same period, whilst the return on total average assets of city commercial banks increased from 1.10% to 1.23%, the overall non-performing loan ratio of city commercial banks decreased from 2.3% to 0.8%. The profitability and asset quality of city commercial banks has improved significantly.

The table below sets out certain information relating to city commercial banks in China for the years indicated:

	For the year ended 31 December				
	2008	2009	2010	2011	2012
	(RMB in billions, except percentage)				
Assets	4,132	5,680	7,853	9,985	12,347
Liabilities	3,865	5,321	7,370	9,320	11,540
Shareholders’ Equity	267	359	482	664	808
Profit after tax	41	50	77	108	137
Non-performance loan ratio	2.3%	1.3%	0.9%	0.8%	0.8%

Source: CBRC 2012 Annual Report; CBRC website

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In recent years, PRC city commercial banks have experienced rapid development. Certain city commercial banks have been restructured, have introduced strategic investors or have sought initial public offerings in order to strengthen their capital base. For example, in 2007, Bank of Nanjing and Bank of Beijing were both listed on the Shanghai Stock Exchange, and Bank of Ningbo was listed on the Shenzhen Stock Exchange. In addition, some city commercial banks have, in accordance with regulations issued by the CBRC, begun developing mix operation business models, such as establishing consumer finance companies and financial leasing companies, and investing in equity interests in insurance companies.

New urbanisation is one of the important components of China's 12th Five-Year Plan. If city commercial banks are able to capture the opportunities brought by such new urbanisation and can leverage their strengths and resources to position themselves well in the market, the total assets and total profits of city commercial banks are expected to grow at a higher rate than other PRC banking institutions.

Increasing Focus on Small and Micro Enterprise Banking

With the improvement of China's economic structure, the strategic status of small and micro enterprises is rising, and the small and micro enterprise banking market is becoming increasingly important.

Since 2007, the PBOC and the CBRC have issued a series of policies and measures to promote lending to SMEs, in particular to small and micro enterprises. Set out below is a summary of the key measures that have been issued:

- In May 2011, the CBRC issued the Notice on Supporting Commercial Banks in Further Improving Financial Services for Small Enterprises (關於支持商業銀行進一步改進小企業金融服務的通知), which encouraged commercial banks to issue financial bonds for the purpose of funding loans to small enterprises (including what are currently referred to as small and micro enterprises). In addition, it adopted specific assessment procedures for loans made to small enterprises and increased tolerance for the non-performing loans ratio of small enterprises.
- In October 2011, the CBRC issued the Supplementary Notice on Supporting Commercial Banks in Further Improving Financial Services for Small Enterprises and Micro Enterprises (關於支持商業銀行進一步改進小型微型企業金融服務的補充通知), which provided more specific regulations and incentive policies such as: (i) giving further encouragement and support to commercial banks to expand their coverage of financial services for small and micro enterprises; (ii) actively supporting the development of small and micro enterprises in technology industries through the creation of innovative systems, products and services; (iii) applying a preferential risk weight of 75% in risk-weighted approach to loans to small and micro enterprises; (iv) applying preferential capital regulatory requirements in respect of loans to small and micro enterprises; and (v) applying a more tolerant non-performing loans ratio to loans to small and micro enterprises. In addition, commercial banks were no longer allowed to charge small and micro enterprises any commitment fee or fund management fee in connection with loans or products offered to them, whilst stringent restrictions were imposed on the charging of financial advisory fees and consultation fees to small and micro enterprises.
- In March 2013, the CBRC issued the Notice on Advancing the Financial Services for Small Enterprises and Micro Enterprises (關於深化小微企業金融服務的意見), which further encouraged and incentivised commercial banks to improve their standard of service, innovate financial products, expand channels of financing, provide integrated financial services to small and

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micro enterprises and expand their financial service network coverage to less developed towns, as well as wholesale markets and trade fairs where small and micro enterprises concentrate. This notice also reinforced the policy that permitted commercial banks to apply to establish several sub-branches in the same city and removed the restriction that banks need a minimum half-year period between two consecutive applications, provided that the number of small and micro enterprises loan customers of such bank and the average balance of loans granted to such customers at the end of each of the previous six months reached certain levels as a proportion of all customers of that bank and the bank's total loan balance (in principle, the relevant levels were set at 70% for eastern coastal provinces and municipalities with independent planning status and 60% for other provinces).

- In August 2013, the CBRC issued the Guiding Opinions on Further Enhancing the Financial Service Work for Small Enterprises and Micro Enterprises (關於進一步做好小微企業金融服務工作的指導意見), which required banking institutions to ensure that (i) the growth rate of loans made to small enterprises and micro enterprises was not lower than the average growth rate for any other type of loans; and (ii) the volume of growth of loans made to small enterprises and micro enterprises was not lower than the corresponding growth rate of the previous year. In addition, the regulations stated that banking institutions would only be entitled to benefit from preferential policies in the following year if they met the above targets and, in particular, granted loans to small enterprises and micro enterprises at a higher rate than the previous year.

In addition, the growing bargaining power of large corporate borrowers, as a result of the gradual liberalisation of interest rates and the increasing availability of alternative financing sources, has partially caused the banking industry to reinforce its focus on small and micro enterprise banking.

As a result of the above, small and micro enterprise banking has grown rapidly in recent years. Loans issued to small and micro enterprises reached RMB14,770 billion as of 31 December 2012, representing an increase of 19.73% from 31 December 2011, and accounted for 21.95% of all corporate loans in China.

Increasing Demand for Personal Finance

There have been significant growth opportunities in the PRC personal finance market due to the increasing consumer demand for more diversified banking products and services, such as residential mortgage loans, credit cards, wealth management services, personal consumption loans and other consumer finance products. The table below sets out the total amount of domestic personal loans and their percentage of total domestic loans for the periods indicated:

	For the year ended 31 December					CAGR (2008-2012)
	2008	2009	2010	2011	2012	
	(in billions of RMB, except percentages)					
Total domestic personal loans	5,706	8,179	11,254	13,601	16,131	29.7%
As a percentage of total domestic loans	18.8%	20.5%	23.5%	24.8%	25.6%	

Source: PBOC

In addition to the traditional personal finance business, a prosperous market for wealth management services has emerged over the past few years as a result of the rapid increase in household disposable income and an expanding class of wealthy individuals. In particular, commercial banks in the PRC have

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started to offer customised and professional services, such as asset management and wealth management services, to mid- to high-end customers.

Following the establishment of private banking businesses in the PRC by some foreign-owned banks, PRC commercial banks have also started to set up their own private banking departments in an attempt to increase their market penetration in private banking services to high-net-worth individuals in the PRC.

Further Expansion of Fee- and Commission-based Business

As the domestic Chinese economy becomes increasingly sophisticated, PRC commercial banks have increased their efforts to provide diversified financial products and services, especially fee- and commission-based products and services.

Historically, commercial banks in China were restricted in their ability to provide fee- and commission-based products and services. Since 2001, however, the Chinese government has issued regulations permitting banks to charge for certain fee- and commission-based products and services. See “Supervision and Regulation – PRC Banking Supervision and Regulation – Pricing of Products and Services”. The contribution from net fee and commission income has increased from 9.7% in 2008 to 13.7% in 2012. It is expected to further increase as domestic banks continue to expand their fee- and commission-based product and service offerings to meet the demand of increasingly sophisticated corporate and personal customers.

Deepening of Interest Rate Liberalisation

Interest rate liberalisation is one of the core parts of economic reform. China has already realised the marketisation of commodities. However, interest rate liberalisation is still lagging behind in terms of reform. Whilst the PBOC has gradually liberalised its regulation of interest rates since 2004, no significant policies of reform were issued between 2004 and 2011. For details on the supervision over interest rates, see “Supervision and Regulation – PRC Banking Supervision and Regulation – Pricing of Products and Services”.

In 2012, the statement by Mr. ZHOU Xiaochuan, president of the PBOC, that “the basic conditions for promoting interest rate liberalisation have been satisfied” indicated that another round of interest rates reform may have been approaching. In April 2012, the PBOC established a working group to analyse interest rate liberalisation (利率市場化改革研究工作小組), which focused on the study of the impact of interest rate reform on, and the development strategy of, the PRC banking industry. On 8 June 2012 and 6 July 2012, the benchmark interest rates for RMB-denominated loans and deposits and the corresponding permitted floating range of interest rates were adjusted twice. The changes allowed banking institutions in China to set minimum interest rates for RMB-denominated loans at 70% of the PBOC benchmark rate and the maximum interest rates for RMB-denominated deposits at 110% of the PBOC benchmark rate. To deepen the interest rate liberalisation, the PBOC further liberalised the control over the lending rate. From 20 July 2013, banking institutions in China are no longer bound by the minimum interest rate threshold for RMB-denominated loans of 70% of the PBOC benchmark rate when setting interest rates on loans they offer. Instead, each banking institution can set the interest rate level at its own discretion (the permitted range of interest rates for personal residential mortgage loans is not adjusted, which still applies the existing housing credit policy). See “Supervision and Regulation – PRC Banking Supervision and Regulation – Pricing of Products and Services”.

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On 25 October 2013, the PBOC announced the introduction of the Loan Prime Rate (“LPR”), which was a new mechanism for the centralisation and publication of LPR quotes. This operates such that on each business day, the first batch of nine quoting banks, which includes the Large Commercial Banks, provide LPR quotes based on the lending rate they offer to their premium clients. The National Interbank Funding Centre, as the designated publisher of the LPR, then excludes the highest and lowest quotes, and calculates a weighted average of the remaining quotes provided by the quoting banks so as to establish an average lending rate which is then published as the LPR rate for that day.

To begin with, only the LPR for loans of one-year maturity will be published. The new LPR mechanism is expected to promote the smooth transition from a pricing mechanism which is determined by the PBOC to a market-based one, thus laying the foundation for further interest rate liberalisation reform.

The on-going interest rate liberalisation may increase pricing competition in the PRC banking industry, but it is also expected to encourage PRC commercial banks to develop more innovative products and services and to adopt risk-based pricing.