

〈Research Article〉

The Reform and the Issues of Chinese Commercial Banks

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Abstract

This paper attempts to start with the history and development stages of China's commercial banks, and summarize and sort out the reform and development process of China's large state-owned commercial banks and joint-stock commercial banks. By tracing back the historical track of the development and changes of China's banking industry, and combining the historical background and policy guidelines of each stage, the impact of China's reform and opening up on China's banking industry is re-examined. After the reform and opening-up, this paper explores the problems existing in various stages of China's banking industry and the internal logic and significance of the reform.

Key words: commercial bank, state-owned, stock-shareholding, ownership structure

1. Overview

1.1 Research background

As an important part of the banking industry, the commercial bank is the crucial leverage in China's pursuit of economic development, and is the main body directly involved in market economy activities. In the early days of the People's Republic of China, China's banking industry was still under unified and backwater management by PBC, while the implementation of the reform and opening up policy by the Chinese government has brought new opportunities for the development of the banking industry.

Over the 40-odd years' of China's reform and opening up, China's commercial banks have scored achievements worldwide as they have doubled their operating performance, asset size, deposit size, and the scale of introducing foreign capital. As of the first quarter of 2019, China's banking industry boasts the total assets of over RMB275.82 trillion (Guo Junhao,2019), ranking the first in the world. Six large state-owned commercial banks, including ICBC and CCB, and four joint-stock commercial banks, including CMB, are on the list of the world's top 500 companies released on July 22, 2019 in *Fortune* [Ma Lin,2019]. However, in the climate of Internet finance, China's commercial banks are encountering new challenges, while deepening reform is essential to maintain competitive edges and improve international competitiveness.

Meanwhile, with the deepening and accelerating development of economic globalization, the financial markets of various countries and regions interact closely. Against the backdrop of new era, new climate and new changes, the reform and development of China's banking industry is at an important turning point. Now, the internal and external environment and business model of China's banking industry bear many new features and are faced with many new problems. These new problems require new ways of understanding and solutions. China's banking industry needs to carry the tough transformation and innovation as well as supply-side reform through to the end (Li Meng ,2018).

This paper attempts to summarize the reform and development process of China's large state-owned commercial banks and joint-stock commercial banks proceeding from the history and development stages of China's commercial banks, and review the impact of China's reform and opening up on China's banking industry through tracing the historical track of the development and changes of China's banking industry, in combination with the historical background and policy guidelines of each stage, as well as explore the problems in all stages and the inherent logic and significance of change.

1.2 Research significance

1.2.1 Theoretical significance

After more than 40 years of development and reform, China's banking industry has made great progress and remarkable achievements. Although there are twists and turns on the road of reform, the overall trend of continuing to improve has maintained. In retrospect of the course of reform, the development experience and the laws of history are summed up objectively in this paper, which can help us to explore the effective ways for the future development of Chinese commercial banks, determine the theoretical basis for the sustainable development of China's banks, clarify the strategic basis for the survival and growth of Chinese commercial banks, conclude the core business of commercial banks, find out the fundamental driving force for the development of commercial banks, and seek the breakthrough point for the development opportunities of commercial banks. In the light of the development law of commercial banks, this paper makes a research and judgment for its future trend, provides development theories of commercial banks in China, further enriches the development theory system of commercial banks in China, and provides the theoretical basis and decision-making basis for the transformation of China's economic development.

1.2.2 Realistic significance

China's banking industry has been playing a leading part in Chinese financial market, holding the key to capital adjustment as credit intermediation, and providing fundamental guarantee for China's economic development. According to the statistics of the China Banking and Insurance Regulatory

Commission, there are 4,588 banking financial institutions in China as of the end of December 2018, including 6 large state-owned commercial banks, 12 joint-stock commercial banks, 134 urban commercial banks, 1,427 rural commercial banks, 17 private banks, 812 rural credit cooperatives and 1,616 village banks in terms of systems (Liu Yajing ,2010). Currently, the structure of China's commercial banks is constantly changing without centralization, and the competition among commercial banks will become ever fiercer. With the deepening of banking market reform, urban commercial banks and rural commercial banks have developed rapidly. At the same time, the establishment of private banks allowed by the Chinese government at the end of 2013 has also broken the inherent structure of the original banking industry, enabling the market to continue to disperse, and stimulating the new vitality of the banking market.

Figure 1 Comparison of the number of financial institutions in China between 2008 and 2018

Classification of equity structure	Category of financial institutions	2008	2018
State-owned capital holding	Policy bank	3	3
	Large state-owned commercial bank	5	6
Non-state-owned capital holding	Joint-stock commercial banks	12	12
	Urban commercial banks	124	134
	Housing saving bank	-	1
	Private bank	-	17
	Rural commercial bank	8509	1427
	Rural cooperative bank		30
	Rural credit cooperative		812
	Rural bank	-	1616
	Foreign legal person bank	29	41

Source: *Almanac of China's Finance and Banking* of 2008 and 2018

1.3 Domestic and foreign research status

Domestic and international scholars have been exploring the development and reform of commercial banks both in theory and practice, trying to seek for new ideas for the development of commercial banks. Most of the existing references are on two main aspects, which are the relationship between commercial banks and economic growth, commercial banks development ideas and reform methods.

1.3.1 Studies on the relationship between the development of commercial banks and economic growth

An array of scholars have always held that the development of commercial banks is closely related to economic growth. Schumpeter (1947) (Liu Wuqiang ,2006) believes that banking institutions with good operating systems can identify enterprises with growth potential through information and data, and empower them to development by providing them with credit loans, thus playing a positive role in sound socio-economic development. It is undoubtable that every coin has two sides. The bad operation of banking institutions will also exert a negative impact on the socio-economic development.

Bernanke (2006) reckons that the bad operation of banks will lead to the failure of excellent entity operators to obtain credit loans to expand their operations or help capital turnover, which will affect the sound development of social economy, and that the bad operation of banking institutions will trigger banking crisis, which will result in economic recession and even economic crisis.

Lin Yifu and Jiang Ye (2006) conducted an empirical analysis through provincial panel data in China. It is concluded that the differences in factor endowment structure, development strategy and economic structure of each province can influence the banking structure of each province, and the more the economic structure inclines to heavy industry, large-scale enterprises and state-owned enterprises, the more concentrated banking structure is.

1.3.2 Studies on bank development ideas and reform method

After the joint-stock system reform of state-owned banks, the development ideas and reform methods of banks have aroused widespread concern of scholars. At present, many scholars discuss the three fronts of system, governance and technology proceeding from macro and micro perspectives, forming three mainstream views, namely, property rights reform view, market structure view and governance structure view.

The view of property right structure is based on the theory of property right structure. It is believed that the relationship between the government and the bank should be clarified by establishing multiple property right subjects with the reform of property right structure as the leading factor. Zhang Jie (1997) believes that the "corporatized" management mode shall be adopted for the reform of state-owned banks to avoid the drawbacks of unclear property rights, low efficiency and loose management of state-owned banks through introducing corporate governance structure and system. Yi Gang and Zhao Xianxin (2011) hold that the successful transformation of modern commercial banks should follow the modern management mode of diversified equity structure and clarified property rights, which can fundamentally solve the soft budget constraint problem of state-owned banks brought about by policy burden. Mi Jianguo, Li Yang and Huang Jinlao (2002) believe that the successful transformation of state-owned banks into commercial banks entails joint-stock reform and disavow the commercial reform method relying solely on increasing incentives.

The view of market structure is based on the theory of industrial organization. It is believed that the holistic efficiency of banking industry should be promoted by introducing competition mechanism and external constraints. Yu Liangchun and Ju Yuan (1999) have analyzed the China's banking industry as a whole with the structure-behavior-performance paradigm and drew a conclusion that the excessively high concentration of the Chinese banking industry caused low efficiency, and proposed suggestions on introducing external competition and opening up the market. Lin Yifu (2011) holds that increasing the market share of small and medium-sized commercial banks is more forward-looking than the reform of state-owned banks. The development of small and medium-sized banks can monitor small and medium-sized enterprises more effectively and improve the efficiency of national economic financing.

The view of governance structure is based on the multi-element and clear equity structure. It is believed that the state-owned banks can take stable steps to achieve the goal of developing into commercial banks by establishing sound rules and regulations. Xu Xiaonian (1999) believes that only by establishing a complete corporate governance system and a rigorous risk management system, can the reform of state-owned banks achieve its desired objectives.

1.4 Research thoughts and methods

The method of the empirical analysis is adopted in this paper to analyze the empirical results and inadequacies of the reform process, centering on the argument, through the retrospect of the reform and development of China's commercial banks. Specifically, this paper analyzes the edges and drawbacks of reform methods of commercial banks in different times in view of the policy factors back then, and studies the motivation of the transformation of the four state-owned banks into large state-owned commercial banks and pertinent reform methods.

2. Initial completion of the banking system (1984–1993)

2.1 Reform of state-owned specialized banks

In December 1993, the *Decision of the State Council on Reform of the Financial System* further clarified that the main function of PBC is to formulate and implement monetary policies and maintain the stability of the value of the currency. It exercises strict supervision over financial institutions to ensure the safe and effective operation of the financial system. The State Council was almost unanimous in that "financial reform should take precedence", and it also set out what still does not seem outdated that "Marketization of interest rates and commercialization of banks." The financial reform started at the end of 1993 can be regarded as a new milestone in the reform of China's banking industry, and the marketing competition of commercial banks has been unveiled since then.

2.2 Successive establishment of joint-stock banks

2.2.1 Establishment of joint-stock commercial banks

From the late 1980s to the mid-1990s, China has set off a wave of the construction of joint-stock banks. With the continuous growth of the economic benefits, the banking system has also begun to actively explore to break the monopoly of state-owned specialized banks. A number of small-scale new commercial banks have been set up by means of guidance from outside the system, and joint-stock commercial banks, urban credit cooperatives and other financial institutions have gradually grown and become an important force in the banking financial system that cannot be ignored.

On April 8, 1987, CMB, the first experimental bank in China to promote banking industry reform from outside the system, was established in Shekou, Shenzhen, the forefront of China's reform and opening up. It was the first joint-stock commercial bank in China wholly owned by business entity, with an exclusive investment by China Merchants Group Shipping Co., Ltd. and a registered capital of RMB100 million. CMB may, with the approval of the PBC, engage in RMB deposits and foreign exchange deposits of individual clients, provide unit call deposits to enterprises and institutions in addition to business of RMB deposits and foreign exchange deposits, and establish a "computer savings card" business. Since then, after two times of capital and stock increase in 1989 and 1994, CMB has evolved from a sole proprietorship of China Merchants Group to a standard joint-stock commercial bank, gradually getting rid of the restrictions of regional commercial banks and moving from Shekou to Shenzhen and from Shenzhen to the whole country.

On January 17, 1989, the PBC approved CMB to increase its capital and expand its shares for the first time, 95% of which were owned by transportation enterprises. At that time, six shareholders, such as COSCO and Guangzhou Maritime Transport Bureau, were newly absorbed. The paid-in capital increased from RMB100 million to RMB400 million, and the sole ownership of China Merchants Group was changed into the joint ownership of six shareholders, forming the organizational structure of joint-stock commercial banks with the nature of limited liability company.

Figure 2 Changes of CMB's Equity in 1989

Shareholder name	Share capital (RMB ten thousand)	Equity ratio
China Merchants Group Shipping Co., Ltd.	18000	45%
China Ocean Shipping (Group) Company	10000	25%
Guangzhou Maritime Bureau of the Ministry of Transport	4000	10%

Shareholder name	Share capital (RMB ten thousand)	Equity ratio
Guangdong Provincial Highway Administration	2000	5%
Shandong Transportation Department Material and Industry Co., Ltd.	2000	5%
Nanhai East Corporation of CNOOC	2000	5%
Qinhuangdao Port Authority	2000	5%

Source: official website of CMB

From May 1989 to early 1993, CMB was in its infancy. During this period, CMB carried out the first capital increase, stock expansion and stock system reform and since then, CMB became a joint-stock commercial bank under the leadership of the Board of Directors, which was wholly owned by the business entity and established the joint-stock enterprise system in the history of the People's Republic of China.

According to the requirements of modern enterprise system, CMB has explored the development path of joint-stock commercial banks, clarified the relationship of property rights, and implemented the separation of real ownership and management rights. It has improved the organization and management system of "first-class legal person and multi-level operation", and established a management system based on the following concept: self-management, at one's own risk, responsibility for one's own profit and loss, self-balance, self-restraint and self-development of the operating mechanism to realize the profit maximization and completely market-oriented behavior.

2.2.2 Establishment of urban credit cooperatives(UCC)

In the late 1970s, with the gradual development of China's economic system reform, a small number of UCC appeared in some regions. China's first UCC were established in 1979 in Zhumadian, Henan Province. Before 1986, there were about 1,300 UCC with total assets of about RMB3 billion. Since the mid-1980s, the establishment of UCC has accelerated, mainly in large and medium-sized cities above the prefecture level, but some places have also established UCC in counties (cities). With the large-scale establishment of UCC throughout the country, in order to strengthen management, the PBC promulgated the Regulations on the *Administration of Urban Credit Cooperatives* in August 1988, which improved the conditions for the establishment of UCC and raised the registered capital from RMB100,000 to RMB500,000. By the end of 1989, the number of UCC had reached 3,330, with a total assets of RMB28.4 billion.

3. Tortuous development of commercialization reform (1994–2002)

3.1 Establishment of policy banks

In 1993, the State Council issued *Decision of the State Council on Reform of the Financial System*, proposing to deepen the financial reform by building the four banks, namely, ICBC, ABC, BOC, CCB, into large state-owned commercial banks, separating the policy-related business from the four banks, and constituting specialized bank especially in charge of undertaking policy-related businesses, namely, policy banks.

Therefore, in order to supplement and perfect the market financing mechanism, induce and restrain the flow of commercial funds, and provide professional financial services, the first policy bank, China Development Bank (CDB), was established in Beijing on March 17, 1994, with a registered capital of RMB50 billion, mainly undertaking domestic development-oriented policy-oriented financial business. The mission of the CDB is to enhance the competitiveness of the country and improve the lives of its people.

On July 1 of the same year, the Export-Import Bank of China (EIBC) was established in Beijing with a registered capital of RMB3.3 billion, mainly to finance the import and export of large-scale mechanical and electrical equipment.

On November 8 of the same year, the Agricultural Development Bank of China (ADBC) was established in Beijing with a registered capital of RMB20 billion, mainly for agricultural policy support.

3.2 Transformation of national specialized banks into state-owned commercial banks

In the initial stage of the planned market-oriented reform, the state-owned banking system has achieved the first transformation, forming a state-owned specialized banking system, providing effective financial support for the smooth transition of the economy. With the deepening of market-oriented reforms and hardness of budget constraint on micro-economic entities, banks and state budgets, the drawbacks of the state-owned specialized banking system are also increasingly exposed. In addition, in order to ensure the smooth completion of the economic transition and the smooth operation of the national economy, the state-owned specialized banks also bear excessive policy burdens and pay a huge price, such as large non-performing loan balance, low capital adequacy ratio, and low economic performance.

Before 2002, the statistics and estimation of the non-performing loan ratio of state-owned banks are incomplete and the standards are not uniform. At that time, according to the *General Rule of Loan* formulated by PBC and the financial accounting system of financial enterprises of the Ministry of Finance of the PRC, the loans are divided into four categories: normal, overdue, sluggish and bad loans. The latter three categories are called non-performing loans, which are called "one overdue-two slacks"

at that time with greater flexibility in identification and operation and lacked relatively accurate figures on the amount of non-performing loans. The reasons of statistics, classification standard and cognition make the society have great differences in the view of the amount of non-performing loans. Still, by and large, the non-performing loan ratios of the big four state-owned banks have been able to collate a number that reflects the changing context. 12% at the end of 1990; 21.4% at the end of 1995. (Bing Li,2018) Therefore, in order to improve the operation of state-owned specialized banks, a two-step approach to the commercialization of state-owned specialized banks has been adopted since 1994.

Step 1: from 1994 to 1997, the state-owned specialized banks should be transformed into solely state-owned banks, and the separation of policy-oriented finance from commercial finance was realized in order to lighten their policy-oriented burden. The state-owned banks should be transformed into independent commercial entities with independent civil capacity and corresponding civil obligations.

Step 2: from 1997 to 2002, the focus of the reform is to reduce the risk of wholly state-owned banks. The state-owned specialized banks have paid a huge reform cost for the smooth completion of the economic transition and the operation of the national economy. As state-owned specialized banks have taken on too much policy burden and simply met the funding needs of domestic enterprises for development, and some did not even conduct market research on capital risks, so they gradually exposed a large number of non-performing loans, and the risks are increasing.

Figure 3 Capital Scale of State-owned Banks, 1998-2002

Item	1998	1999	2000	2001	2002
I. Deposits	69782.2	79973.5	90892.7	97346.9	113452.28
1. Enterprise deposits	25249.1	28733.1	33337.6	33081.3	35980.06
(1) Current deposit	19146.1	21810.4	25585.4	25192.8	27546.94
(2) Fixed deposit	6103.0	6922.7	7752.2	7888.5	8433.12
2. Fiscal deposit	2169.6	2106.3	3477.3	3330.6	3447.90
3. Deposits of institutions	1215.6	1720.3	2079.4	2493.6	4610.00
4. Urban savings deposits	39561.0	44828.0	48626.8	54306.9	64024.46
(1) Current deposit	8722.2	11225.3	14043.9	16626.6	20893.90
(2) Fixed deposit	30838.8	33602.7	34583.0	37680.2	43130.56

Item	1998	1999	2000	2001	2002
5. Agricultural deposits	300.6	342.1	372.0	409.7	465.72
6. Other types of deposits	1286.3	2243.7	2999.6	3724.8	4924.14
II. Financial bonds	1.7	1.4	1.0	0.8	0.47
III. Inter-bank transactions	2706.0	3137.8	6141.0	5870.9	5055.76
IV. Cash in circulation	11204.2	13455.5	14652.7	15688.8	17278.03
V. Liabilities to international financial institutions	174.4	371.9	368.3	484.5	423.05
VI. Miscellaneous	6997.3	4228.9	-1927.1	-967.7	963.86
Total funding sources	90865.8	101169.0	110128.6	118424.2	137173.46
I. Deposits	68442.1	73695.8	76393.8	80077.6	90892.63
1. Short-term loan	48105.7	50113.2	49242.1	43679.8	45800.67
(1) Industrial loan	16664.1	16786.5	15657.7	15763.2	16745.38
(2) Commercial loan	18746.7	18989.5	16958.5	16463.5	15760.12
(3) Construction loan	1512.4	1322.8	1425.6	1684.8	2168.03
(4) Agricultural loan	1781.6	1744.6	1289.4	1272.3	1286.04
(5) Loan to township enterprise	1754.9	1905.4	1415.3	1450.5	1542.61
(6) Loan to foreign-funded enterprises	2226.9	2675.5	2678.3	2392.2	1723.46
(7) Loan to private enterprises and individual	208.3	301.0	354.4	425.9	392.42
(8) Other short-term loans	5210.8	6387.9	9462.9	4227.4	6182.61
2. Medium and long term loan	19744.3	22791.7	26406.1	34995.7	42317.21

Item	1998	1999	2000	2001	2002
3. Other types of loans	592.1	790.9	745.6	1402.1	2774.75
II. Portfolio and investment	6037.6	9675.0	16419.4	16913.4	19488.39
III. Inter-bank transactions	669.6	928.1	941.6	1153.7	1060.85
IV. Funds outstanding for gold and silver	12.0	12.0	12.0	256.0	337.24
V. Funds outstanding for foreign exchange	13660.6	14671.9	14203.5	17687.3	23014.07
VI. Financial loan	1582.1	1582.1	1582.1	1582.1	1582.06
VII. Assets at international financial institutions	461.8	604.1	576.3	754.2	798.22
Total use of funds	90865.8	101169.0	110128.6	118424.2	137173.46

Source: *Almanac of China's Finance and Banking 1999-2003*

With the outbreak of the Asian financial crisis in 1997, a large number of enterprises were affected by the financial crisis. The domestic financial market was also hit hard, and the non-performing loan crisis accumulated by state-owned banks for a long time was gradually exposed, which also made the risks faced by state-owned banks more prominent. From 1998 to 2002, the state adopted a series of reform measures to reduce the risk of state-owned banks, replenish the capital for state-owned commercial banks and strip off non-performing loans. In January 1998, the Ministry of Finance first issued RMB270 billion in special bonds to inject capital into the four banks. Among them, ICBC of RMB85 billion, ABC of RMB93.3 billion, BOC of RMB42.5 billion, and CBC of RMB49.2 billion. After completion in June, the capital adequacy ratios of the banks reached the standard.

However, this stage of reform has improved the quality of assets and capital adequacy ratio of banks to a certain extent and the ability of state-owned banks to resist risks, but it has not fundamentally solved the soft budget constraints of state-owned banks caused by the policy burden. In 2000 and 2001, the non-performing loan ratio of state-owned banks reached 55.11% and 49.29% respectively after excluding the policy divestiture factor. The non-performing assets of state-owned banks have exceeded

their own capital and are in the state of "technical bankruptcy" in essence. So far, the reform of state-owned commercial banks has fallen into a dilemma.

3.3 Rapid development of joint-stock banks

After the 14th National Congress of the Communist Party of China in 1992, the construction of economic system and legal system was strengthened, and the *Law of the People's Republic of China on the People's Bank of China* and the *Law of the People's Republic of China on Commercial Banks* were promulgated one after another, which provided the legal guarantee for the independent operation, self-risk and self-profit and loss of the commercial banks.

Under the supervision and support of the PBC, the joint-stock commercial banks have devoted a lot of energy to standardizing the corporate governance structure, improving the effectiveness and professionalism of internal management. (Zhang Jie,1998)

3.4 The emerging of urban commercial banks (UCB)

UCB are formed under the special historical conditions of China. They are the products of the central financial authorities in rectifying UCC and resolving local financial risks. Since 1995, the first UCB in China-Shenzhen Urban Cooperation Bank (now Ping An Bank) was established. The establishment of UCB has gradually changed the widespread problems of urban credit cooperatives such as decentralized operation, small capital scale, weak ability to resist risks and so on, and further strengthened the construction of the organizational system of commercial banks. However, in the early period of UCB, the risks and weaknesses accumulated in the past have not been fully exposed, resulting in the lack of management of some branches of commercial banks, imbalanced development of various regions. As a special group, UCB have the following characteristics in scale and operation: First, small overall scale. Due to its geographical constraints, the assets of UCB in China are generally small. Secondly, highly dependent development. According to a survey in 2004, UCB with good performance are mainly concentrated in the more developed areas, especially in the eastern China. Third, unclear market positioning. At the beginning of its establishment, the urban commercial bank had established the market orientation of "serving the local economy, the small and medium-sized enterprises and the urban residents" However, there are still a considerable number of UCB show the vacillating market positioning.

3.5 Reform of rural credit cooperatives (RCC)

RCC are cooperative financial organizations which are composed of farmers' shares, democratically managed by their members, and mainly serve them. They are formal financial institutions approved by PBC in accordance with the law. The so-called bank financial institutions are also called deposit-taking

institutions and deposit money banks. Their common characteristics are to take deposits as the main liabilities, to issue loans as the main assets, to handle transfer and settlement of accounts as the main intermediary business, and to directly participate in the creation of deposit money.

Since 1996, when the State Council decided to decouple the RCC from the ABC, the RCC have begun to operate through cooperation. In August 1996, the State Council issued the *Decision of the State Council on the Reform of Rural Financial System*, stressing that the focus of the reform is to reform the management system of rural credit cooperatives and transform them into real cooperative financial organizations. After the reform, the governance model of RCC has undergone fundamental changes, the long-standing problem of insider control has been effectively solved, and the organizations themselves have formed an endogenous driving force to further promote the reform of institutional mechanisms.

4. Dividend Release Phase in Joint-stock Reform (2003–2013)

4.1 Joint-stock reform and listing of China's four major banks

After 2003, with the further market-oriented reform, China has entered another period of rapid economic growth, with GDP growth in double digits in most years, relaxed market environment, sufficient liquidity and high M2 growth rate. After the financial crisis broke out in 2008, China launched a RMB 4 trillion economic stimulus plan, which commercial banks were not negatively affected, but seized the opportunity. The favorable domestic macroeconomic conditions provide a good external environment for the rapid development of commercial banks, and realize the rapid expansion of assets and profits. During this stage, China's banking industry has achieved rapid development. Its capital quality, non-performing loan ratio, liquidity ratio, profitability and other indicators continue to improve, and gradually narrow the gap with the world's first-class banks, or even catch up with the advanced international banks. These good performances are the result of the dividend release.

Figure 4 Capital Utilization of the Four Major Banks in 2003-2015

Item	2003	2004	2005	Growth Rate
Net Foreign Assets	37732.92	55348.92	75595.86	100.34%
Domestic Credits	206283.64	225261.84	248367.10	20.40%
Claims on Government (Net)	13178.51	15495.74	15197.27	15.32%
Claims on Non-	172700.24	192983.35	209502.94	21.31%

Item	2003	2004	2005	Growth Rate
financial Sector				
Claims on Other Sectors	20404.89	16782.75	23666.89	15.99%
Currency and Quasi-money	221222.82	254106.95	298755.67	35.05%
Currency	84118.57	95969.72	107278.76	27.53%
Cash in Circulation	19745.99	21468.30	24031.67	21.70%
Current Deposit	64372.58	74501.42	83247.09	29.32%
Quasi-money	137104.25	158137.23	191476.91	39.66%
Fixed Deposit	20940.39	25382.15	33099.99	58.07%
Saving Deposit	103617.65	119555.39	141050.99	36.13%
Other Deposits	12546.21	13199.69	17325.93	38.10%
Deposits in Foreign Currency	11884.29	12129.83	12358.60	3.99%
Bond	11653.96	15203.49	20378.79	74.87%
Central Bank Bonds	0.00	0.00	0.00	0.00%
Paid-up Capital	10949.09	11969.42	14252.11	30.17%
Others (net)	(11693.61)	(12798.94)	(2178221)	185.27%

Source: China Financial Yearbook 2004-2006

The state has promoted a new round of reform of commercial banks by combining stock adjustment with incremental reform. On the one hand, the National Financial Work Conference of the CPC Central Committee held in 2002 clearly made the reform of state-owned banks the top priority of the national financial reform. According to the modern commercial bank system, the state-owned banks should be reformed into joint-stock commercial banks, the property right structure should be optimized, the policy burden should be lightened, the state credit should be promoted, the state-owned banks should be established into joint-stock commercial banks in general sense. At the same time, it is clearly put forward that the mature joint-stock commercial banks should be listed..

The four state-owned banks have successively completed the shareholding system transformation,

and then listed in public, becoming publicly-owned banks which are subject to social supervision; Secondly, in the light of the relevant provisions of Articles 54 and 55 of Chapter V of the Commercial Bank Law (Revised 2003), commercial banks shall establish and improve their own financial and accounting systems in accordance with the law and the unified accounting system of the State and the relevant regulations of the banking supervision institution of the State Council. A commercial bank shall, in accordance with the relevant provisions of the State, truthfully record and comprehensively reflect its business activities and financial situation, prepare an annual financial accounting report, and promptly submit it to the banking supervision institution of the State Council, the People's Bank of China and the financial department of the State Council. These relevant laws and regulations improved corporate governance and management capabilities from the institutional level; Thirdly, the bank introduces foreign strategic investors in line with its own situation and the scope of business.

Figure 5 Introduction of Foreign Investment by the Big Four Banks, 2003-2009

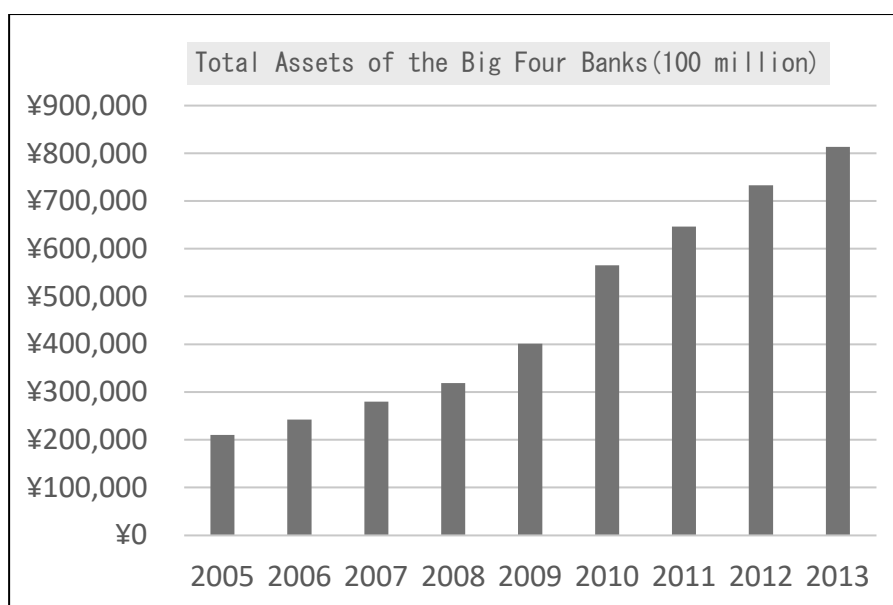
Item/year	2003	2004	2005	2006	2007	2008	2009	2009
	Balance	Accumulated Data of the Current Year	Accumulated Data of the Current Year	Accumulated Data of the Current Year	Accumulated Data of the Current Year	Accumulated Data of the Current Year	Accumulated Data of the Current Year	Balance
Number of Chinese Banks Introducing Overseas Investment	5	6	7	6	5	6	0	31*
Amount of Introduced Investment (unit: USD 100 million)	2.6	23.5	116.9	52.2	17.6	115.2	2.1	329.9
Funding Amount for Overseas Listing	-	-	113.9	299.0	42.2	0	39.3	494.3
Total	2.6	23.5	230.8	351.2	59.8	115.2	41.4	824.2

Source: The CBRC's 2009 annual report * shows that the figures differ from the sum in the table.

Meanwhile, the state-owned commercial banks also introduced advanced technology and management experience from abroad by "attracting foreign investment" in the process of excessive transformation.

This new round of reform, with the reform of property rights as its core, the reform of shareholding system as its symbol and the establishment of modern commercial bank system as its goal, has basically realized its original intention. By introducing market competition and updating the ownership structure of state-owned banks, the Chinese government enables commercial banks to have rigorous and efficient internal management processes. The finance of state-owned banks has been restructured through write-off, capital injection, debt issuance, the introduction of foreign capital, which invigorates their operating capacity. During this period, the asset quality of state-owned commercial banks has increased, the banks' profitability improved, and their non-performing loan ratio decreased. At the same time, the state-owned banks were quickly recognized by the international community. By the end of 2013, the total assets of the four state-owned banks had their total assets reached RMB81.39 trillion, which is four times the total assets of 2003; On the other hand, the market-oriented commercial banking system will be established through further enriching the market players and improving the competitiveness of the banking industry.

Figure 6 Total Assets of the Big Four Banks, 2005-2013



Source: China Financial Yearbook, 2006-2014

4.2 "Upgrading and transformation" of Joint-stock Banks

Since 2003, small and medium-sized banks have entered the golden development period, the national joint-stock commercial banks have expanded again, and HengFeng Bank(HFB), China Zheshang

Bank(CZB) and China Bohai Bank(CBHB) have either been restructured or newly established. The market share and the number of institutions are booming, and their asset shares in banking financial institutions are also increasing.

The national joint-stock banks adhere to the combination of internal and external opening up. By introducing foreign strategic investors and institutional investors, they have publicly listed at home and abroad, which has perfected the national network.

In the meantime, joint-stock commercial banks have also stepped forward for public listing. In this way, the joint-stock commercial banks not only supplement the capital, but also increase the degree of equity dispersion, which make them well-known at home and abroad. Shenzhen Development Bank Co., Ltd. (stock abbreviation: SDB A, stock code: 000001) was the first commercial bank in China to issue its shares and go public. Afterwards, the joint-stock commercial banks such as SPD Bank, CMBC and CMB were listed successively, which made it possible for the inflow of funds. After listing, the scale of joint-stock commercial banks expanded rapidly. CMB as an example, in 2013, the CMB had 113 branches and 934 outlets in 110 cities, while in 2003, the number of outlets was only 373.

At the same time, joint-stock commercial banks pay attention to technological innovation and introduction, constantly launching new financial products and optimizing income structure. The market value is widely recognized.

Figure 7 Listing Process of Joint-stock Commercial Banks from 2003 to 2013

Date	Bank	Transaction Place
April 3, 1991	SDB (the current Ping An Bank)	Shenzhen Stock Exchange (A-shares)
September 23, 1999	SPD Bank	Shanghai Stock Exchange (A-shares)
December 19, 2000	CMBC	Shanghai Stock Exchange (A-shares)
April 9, 2002	CMB	Shanghai Stock Exchange (A-shares)
July 21, 2003	Hua Xia Bank(HB)	Shanghai Stock Exchange (A-shares)
September 22, 2006	CMB	Hong Kong Stock Exchange (H-Shares)
April 19, 2007	CITIC Bank	Shanghai Stock Exchange (A-shares)
November 26, 2009	CMBC	Hong Kong Stock Exchange (H-Shares)
August 19, 2010	China Everbright Bank(CEB)	Shanghai Stock Exchange (A-shares)

In December 2002, SPDB and CitiBank signed the Strategic Cooperation Agreement, and the two sides agreed to carry out strategic cooperation in corporate governance, audit compliance, risk management, restructuring, business development and other aspects. SPDB hopes to introduce strategic investors and exchange technology, management, market and products from the world famous banks with a small amount of equity (4.62% of CitiBank's equity participation), to make the bank bigger and stronger quickly, which will be invincible in the fierce competition market and develop into a better international commercial bank in the next decade. In comprehensive management and international development, CITIC Bank will take advantage of the unique CITIC Financial Integrated Management Platform and the "trinity" strategic system formed with BBVA Bank of Spain and CITIC International Financial Holding Company, so as to foster comprehensive and international management characteristics. In 2006, CITIC Bank transferred 5% of its equity to Spain's BBVA Bank for EUR500 million, successfully attracting international strategic investors. After that, BBVA Bank increased its holdings and now holds 15% of CITIC Bank, becoming the second largest shareholder of CITIC Bank. In addition, BBVA Bank and CITIC Bank cooperate in risk management, financial services, cash management, fund custody, auto finance, private banking, capital and other business areas.

Almost all joint-stock banks have set their strategic goal of becoming better international banks and developed an internationalization strategy. However, in view of the existing international environment, CMB is clearly in the forefront, mainly in the acquisition of Wing Lung Bank of Hong Kong, the establishment of a Hong Kong branch, a New York branch and a representative office in London, and the establishment of branches in almost all international financial centers. But the proportion of its foreign assets is still very low, so it cannot be called an international commercial bank yet. The internationalization strategy of other joint-stock banks is in progress. In the long run, internationalization strategy is helpful to develop the bank's international business and enhance its brand influence.

5. Transition and Development Stage under the New Normal of Economy (2014 – present)

5.1 Challenges for Commercial Banks under the New Normal of Economy

First, facing the challenge of changing the traditional banking management philosophy under the high-speed growth model. At present, new changes have taken place in the economic environment on which China's banking industry depends, a moderate growth rate of around 7% will become the new normal of China's economy. In order to adapt to the long-term medium-speed economic growth environment, the banking industry should make corresponding adjustments and changes under the high-speed economic growth environment.

Second, they are faced with the challenge of boosting economic restructuring and upgrading and enhancing the ability of serving the real economy. Under the new normal of economy, the financial

industry will give full play to its leading and supporting role in adjusting the economic structure and upgrading the industrial level. Through effective resource allocation, it can fully meet the financial services requirements in line with the new normal, especially to address the long-standing problems of inadequate financial services for small and micro enterprises, agriculture, rural areas and other fields, high social financing costs, and difficult access to financing.

Third, facing the pressure of asset quality rebound, especially the challenges of regional risk accumulation. For a long time, the non-performing loans in China's banking industry have maintained a good situation of "double-decline" for a long time. In 2012, the asset quality of China's banking industry reached the highest level in history, and the non-performing loan ratio remained at the lowest level of 1% in history. Influenced by the slowdown of economic growth, the acceleration of deleveraging and de-bubbling, and the overcapacity of some industries, the non-performing loan ratio of China's banking industry is in a recovery state. Although China's banking industry is fully prepared for this, including a high level of capital adequacy (about 12%) and provisioning coverage (about 250%), the full exposure of regional financial risks to the banking industry can't be excluded. It can be expected that under the new normal of economy, with the passage of time and the pace of economic restructuring accelerated, asset quality is facing greater pressure of rebound, and how to prevent the financial risks that may arise from this become a real challenge in front of China's banking industry.

5.2 The Transformation of Commercial Banks under the New Normal of Economy

5.2.1 Adjustment of customer structure and enhancement of the development of small micro and retail customers

With the diversification of financing channels, the dependence of large enterprises on bank loans has decreased significantly, and the bargaining power of banks has also been affected to a certain extent. On the other hand, with the accumulation of personal wealth and the change of consumption habits in China, the demand for financial services in the residential sector is expanding rapidly in scale, while the types of demand are becoming increasingly diverse. From the traditional consumer credit to the emerging wealth management, it provides a new development space for banks.

Faced with rising capital costs, most banks are turning to customers with more room to negotiate in order to maintain net interest margins. In addition, at the regulatory level, commercial banks have increased the adjustment of credit customer structure in the past few years, and generally increased investment in small and micro enterprises and retail customers, due to the inclination to small and micro enterprises and retail enterprises in capital regulation requirements (lower risk weight). By the third quarter of 2014, more new loans from commercial banks had gone to personal loans, accounting for more than 30 per cent. While the share of new loans in traditional credit facilities, such as the

wholesale and retail sectors and the manufacturing sector, declined significantly.

5.2.2 Adjust the income structure to continue to increase the proportion of non-interest income

The narrowing of net interest margin has a great impact on the profitability of banks. In order to expand the sources of income, banks have generally accelerated the development of intermediary business. Since 2010, the proportion of non-interest income of commercial banks has been rising steadily. By the third quarter of 2014, the average proportion of non-interest income of the whole industry has reached 22.01%, which has become the main driving factor to maintain the growth of bank's net profit. From the data of listed banks, the proportion of non-interest income of all kinds of banks has increased. Comparatively, the proportion of intermediate business income of large state-owned banks (especially BOC) has been maintained at a high level in the industry, and the growth is relatively slow. In the past few years, the income structure of the joint-stock banks and some city commercial banks has changed obviously, showing a large increase.

5.2.3 Adapt to the adjustment of the business model and optimize the organizational structure

With the continuous expansion of scale and increasing complexity of business, the management structure of large banks shows a series of disadvantages, such as low management efficiency, slow market response, rigid risk control and so on. The adjustment of customer structure and business structure has in fact put up with more requirements for banks: on the one hand, specialization and standardization can improve management efficiency and manage risks better; on the other hand, the customer-centered personalized service requires differentiated innovation abilities from banks. How to find a better balance between these two seemingly contradictory trends will be the goal and direction of bank organizational and management structure adjustment.

5.2.4 Differentiated operation to stabilize customers

With the increasingly fierce competition in the same industry, differentiated operation has become another important way of the banking transformation. Through differentiated positioning for customers and product, different types of banks can fully take their advantages and better meet the financial needs of the target customers. Specifically, large banks should develop all businesses in an all-round and coordinated way and build up comprehensive banks featuring comprehensive and international operation, relying on their huge scale of asset liabilities, extensive network layout, huge customer resources and full coverage of financial channels. At the same time, in the framework of integrated management, with the help of the concept and mode of characteristic management, relying on characteristic business and some areas of characteristic management, they should follow the way of characterization. On the other hand, small and medium-sized banks should feature professional

operation, give full play to their advantages such as simple and flexible organizational structure, sensitive information and close to customers, and pay attention to "being perfect and detailed" instead of "being enlarged and fulfilled". Small banks focus on small and micro enterprises, on the basis of the community and local development to provide fast, flexible and characteristic financial services, in order to become regional banks in an all-round way, characteristic boutique banks and even specialized banks, finally creating a "blue ocean" in the fierce competition.

At present, China's economic situation is in a stage of steady development. The tide of supply-side reform implemented by Chinese government and the open attitude for the banking industry market will bring opportunities and challenges to the future development of Chinese commercial banks. Under the current situation of financial reform, China's banking industry is facing a common problem about how China's commercial banks assess the situation and grasp the good developmental opportunity. This paper studies the advantages and problems of China's commercial banks in the reform process by tracing back to the reform process of China's commercial banks and analyzing their reform strategies. Through summarizing and learning from the experience and combining it with the current environment, this paper researches and judges the future development trend of China's commercial banks, aiming at providing suggestions and directions for the development of China's commercial banks at the level of government policies formulating strategies and countermeasures at the level of commercial banks themselves.

Throughout the various stages of China's reform into its commercial banks, there are prominent features in each stage. In the first stage of transformation, the financial system with national specialized banks as the theme was formed, and from then on, the banking system of China realized the transformation from a unified banking system to one with four state-owned specialized banks as the main body. In this process, the share of the state-owned financial system in the mobilization and allocation of economic resources has been increasing, the scale of state-owned banks has expanded greatly, and the credit funds of state-owned banks have gradually become the main source of funds for the development of state-owned economy. In the initial stage of a market-oriented reform of the planned economy, the state-owned banking system achieved its first transformation, providing effective financial support for the stable transformation of the economy. As the development of market-oriented reform deepens, the drawbacks of the state-owned specialized banking system are increasingly surfacing due to the hardening of the micro-economic subjects, banks and the national budget constraints, thus leading to the second transformation of the state-owned banking system. In this stage, the state-owned banks have undergone commercial reforms. After the two transformations, the state-owned banks began to move towards the standard commercial banks in appearance, with the efficiency orientation as the keynote of the transformation. Despite the success of the second transformation, many advanced ideas and methods have been introduced into the management of

banks, operating performance and internal risk control mechanisms have been gradually established, and external administrative intervention is obviously weakened, but overall, these measures focus on technical improvements like combing the internal and external relations, introducing advanced management technology, and dealing with non-performing assets, which are far from fundamentally reversing the operating mechanism of state-owned commercial banks, so the problem of the huge non-performing loans caused by the low efficiency of state-owned banks is still very prominent. Under the internal pressure from the economic reform entering a critical period and the external pressure from international competition after China's entry into WTO, this huge transformation cost urgently needs to be digested and solved. In the past, the reform of state-owned banks emphasized the efficiency guideline, but there were no profound problems such as the real primary system. In the third phase of the reform, the general goal of the comprehensive reform of state-owned commercial banks is clearly defined. The state-owned specialized banks have been transformed into modern joint-stock commercial banks with sufficient capital, strict internal control, safe operation, better services and benefits, and international competitiveness by tightly grasping the central links of reform of the management system, perfection of governance structure, transformation of the operating mechanism and promotion of performance progress. Therefore, the third stage of the systematic transformation of state-owned commercial banks is a fundamental system reform, a comprehensive reform ranging from the internal property rights, governance structure and other related operation and management mechanisms to the external related supporting mechanisms.

The deficiencies of this study are: First, based on the fact that the development of commercial banks in the new economic context is still in the initial stage of research and development, this study analyzes and discusses the government policy and the plan for strategic development of commercial banks, but does not carry out in-depth and detailed study into a commercial bank based on its development status, thus it is unable to give commercial banks enforceable rules. Second, the lack of information disclosed from commercial banks affects the selection of research data. Third, the obvious differences in the development of China's commercial banks make it impossible to conduct a detailed study of the development and reform strategies.

Further research will focus on the following: First, enrich the sample data of the research objects, and analyze the advantages and disadvantages of commercial banks in various forms of business through field investigation and data collection. Second, through data comparison, increase the differentiated outlets of commercial banks, and find out the development direction of the differential operation.

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Note:

- (1) [D]:Dissertation
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- (3) The list of the world's top 500 companies released on July 22, 2019 in *Fortune*:
http://www.fortunechina.com/fortune500/c/2019-07/22/content_339535.htm
- (4) [N]:News