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Iftekhar Hasan and Ru Xie

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Iftekhhar Hasan* and Ru Xie#

A note on foreign bank entry and bank corporate governance in China

Abstract

China employs a unique foreign bank entry model. Instead of allowing full foreign control of domestic banks, foreign investors are only permitted to be involved in the local banks as minority shareholders. At the same time, foreign strategic investors are expected to commit to bank corporate governance improvement and new technology support. In this context, the paper examines the effect of foreign strategic investors on Chinese bank performance. Based on a unique data set of bank ownership, performance, corporate governance and stock returns from 2003 to 2007, our regression and event study analysis results suggest that active involvement of foreign strategic investors in bank management have improved the corporate governance model of Chinese banks from a control based model to a market oriented model, and accordingly have promoted bank performance.

JEL Classification Code: G21, G28, G34, F23

Keywords: China, Foreign Market Entry, Corporate Governance

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1 Introduction

Earlier studies suggest that foreign investment in Chinese banks can improve domestic bank performance. Using a panel of Chinese banks over the 1994–2003 period, Berger, Hasan, and Zhou (2009) find that banks undergoing foreign acquisition record improved efficiency. This paper extends further by investigating not only the effect of foreign strategic investments in Chinese banks, but also the reason why foreign minority investment has influenced the prudent behaviour of domestic banks. Generally, foreign bank entry brings two effects to the domestic banking market. One is increased bank competition and the other is the potential adoption of a better bank corporate governance system as well as other institutional environment reforms. The foreign bank entry regulation in China is distinctively different from that of other countries, with very restrictive green field investment constraints and very low foreign ownership caps. For this reason, the direct competition effect from foreign banks is very limited in China. This distinctive entry model in China provides us with a unique sample for an investigation into the role of corporate governance during foreign banks' presence in developing countries. We test whether foreign minority ownership involvement can improve the domestic bank corporate governance system – using data from a developing country - and whether the change in corporate governance will influence bank performance.

Earlier literature observes that through cross-border mergers and acquisitions, target firms will adopt better corporate governance systems from the acquiring firms (Bris, Brisley, and Cabolis, 2008). Also, international mergers and acquisitions have an impact on cultural integration in the form of cultural convergence (Sarala and Vaara, 2009). In an empirical study, Douma, George, and Kabir (2006) find that the documented positive effect of foreign ownership on firm performance is substantially attributable to foreign corporations with longer-term management involvement. In a recent study, Kang and Kim (2010) argue that foreign acquirers are more likely to engage in post-acquisition governance activities with fewer information asymmetries. Therefore, foreign bank entry into developing countries through mergers and acquisitions is expected to increase the governance quality of domestic banks. However, the important role of corporate governance is, unfortunately, not widely discussed in the earlier foreign bank entry studies, partly because of data constraints.

In this paper, we manage to collect data on four aspects of the corporate governance performance of all key Chinese banks during the 2003-2007 period on bank ownership, board composition, bank risk management, and CEO compensation. Based on the manually collected corporate governance variables, two corporate governance indices for each bank are constructed. We trace the direct effect of foreign involvement on bank performance finding that foreign investors mitigate bank risk taking. The results also reveal that foreign minority investment influence improved corporate governance of participating partner banks and such foreign strategic investments are rewarded in the capital market.

The remainder of the paper is organized as follows. Section 2 discusses the effects of foreign bank presence on the Chinese bank corporate governance system. In section 3 we conduct a regression analysis to investigate the consequential effects of foreign strategic investment and corporate governance transition on bank risk taking. In section 4, an event study analysis is performed to investigate the market reactions of foreign strategic investments on domestic banks and section 5 concludes.

2 Corporate governance of chinese banks

Foreign strategic investment started in China in 2001, when the International Financial Corporation (IFC), the private sector arm of the World Bank Group, first took 7 percent stakes in the Bank of Shanghai, a city commercial bank in China. From 2003 to 2007, during the restructuring of major Chinese banks, there was a boom for foreign bank investments in China. The original intention of introducing foreign strategic investors was to promote diversification of investment, accelerate the improvement of the corporate governance structure, and increase the capital adequacy ratio and IPO value. Until the end of 2008, 21 Chinese banks, including 3 of the big 4 state-owned bank, 10 national joint stock banks, and 8 city commercial banks, altogether introduced 25 foreign strategic investors.

Before foreign investment, the corporate governance model of Chinese banks was characterized as a control-based corporate governance model. In a control-based model, the controlling shareholders – in most cases, the state – employ all feasible governance mechanisms to control the banks tightly. A concentrated ownership structure, management-friendly boards, inadequate risk management disclosure, and non-performance-

related CEO compensation were the standard governance practice commonly observed among the Chinese banks, especially the non-listed state-owned banks. The control-based governance model has demonstrated many built-in weaknesses, which make it less effective in disciplining controlling shareholders and fostering banks' long-term performance. However, the market-oriented governance model refers to a governance model in which market-based mechanisms are used to resolve agency problems. The market-based mechanisms include dispersed ownership, an independent board, a high level of information disclosure, and performance-related CEO compensation. Table 7, in the appendix, summarizes the characteristics of the these two corporate governance models implemented before and after foreign strategic investments.

The penetration of foreign banks is expected to lead the corporate governance reform of Chinese banks. Foreign strategic investors could contribute to the Chinese corporate governance reform through both ownership and management participation. Taking stakes in Chinese banks will diversify the former concentrated ownership structure of domestic banks. The more diversified ownership structure should increase the pressure on banks to improve their internal governance systems. At the same time, direct involvement in bank management through the occupation of one or two seats on the management board will enhance information transparency and strengthen bank management. From 2003 to 2007, accompanied by the rapid growth of foreign bank ownership participation, the former corporate governance structure of major Chinese banks changed substantially. The major Chinese banks with foreign partners experienced a transition of the corporate governance model, from the earlier control-based model to a market-oriented model. The earlier highly concentrated ownership structure, especially of those 100 percent state-owned banks, became diversified due to foreign bank ownership participation and public listing. The more diversified ownership structure increased the pressure on banks to set up a modern management board structure. Chinese banks employ a two-tier board system consisting of both a management board and a supervisory board. Since 2003, the bank board size has been substantially improved to consist of both executive board members and non-executive board members. Shortly before the foreign investments, an independent board system was introduced to the major Chinese banks to provide a consulting function for bank management and to protect the interests of small and medium-sized investors. Foreign strategic investors also have the right to nominate one or two board members. The board of directors of the Bank of China, for instance, now consists of 16 directors, of which 4 are foreign

shareholder nominated board members and 4 are international senior financial experts serving as independent directors. Furthermore, an independent risk management committee was established directly under the management board in most Chinese banks shortly after the foreign strategic investments. In most cases, with concerns about the Chinese bank risk management weakness, the foreign board members take one or two seats on the newly established independent risk management committee to enhance the information transparency of bank risk management.

3 Regression analyses

Our sample is composed of annual data for 30 Chinese banks over the period 2003–2007. The sample of 30 Chinese banks contains all the 4 big state-owned banks, 12 of the 13 national joint stock banks, and 14 of the 112 city commercial banks. Among them, 20 banks had already introduced foreign strategic investors prior to the end of 2007 and 10 banks are without foreign ownership participation. Our sample represents the main universe of Chinese banks, accounting for over 70 percent of the total banking system assets. Since for some of the banks we do not have information for every year, our data contain a total of 110 observations. We first investigate the role of foreign strategic investment in domestic bank prudent behaviour. In this case, we need to approximate banks' risk and foreign ownership participation. In our analysis we use the ratio of non-performing loans to approximate a bank's exposure to credit risk. A higher ratio of non-performing loans represents less prudent lending behaviour and higher concerns of bank risk. We apply three proxies for foreign investments. A dummy variable of whether the bank has a foreign strategic investor, the percentage of foreign strategic investment in a Chinese bank, and a dummy variable of whether the foreign strategic investor has a stake of more than 10 percent in a certain bank are implemented to approximate the foreign participation in Chinese banks. Furthermore, we include the bank size and bank equity ratio as bank-specific control variables. Bank size is defined as the natural logarithm of the total assets and is used to control different characteristics between relatively large and small banks, as well as the economies of scale. Banks with a lower equity ratio might reflect a lower risk aversion of the management and control of this variable could adjust the possible bias of the final results we

estimate. All these bank-level variables are obtained from bank annual reports. Finally, bank performance and risk-taking behaviour could be influenced by the general macroeconomic conditions besides foreign ownership participation and other bank-specific characteristics. To control for these macroeconomic effects, we include the inflation rate and the annual GDP growth rate in all the regression models. The macroeconomic information is drawn from the Chinese Central Bank database.

The OLS estimation results, shown in Table 2, indicate that foreign ownership participation is negatively and significantly associated with bank non-performing loan ratios.¹ The first column, with the dummy variable of foreign strategic investment as the independent variable, shows that banks with foreign strategic investments enjoy lower non-performing loan ratios. We then apply the percentage of foreign strategic investment as the independent variable and the results remain. The last column contains results with the independent variable of whether the foreign strategic investor has a stake of more than 10 percent in a certain bank. The average foreign investment in Chinese banks is as low as 6.92 percent of the bank total assets. Therefore, in the last specification we test whether higher foreign bank ownership control is associated with more prudent behaviour for domestic banks. The results, once again, exhibit significant and negative coefficients, suggesting that a higher investment will significantly mitigate bank risk-taking incentives. As shown, all three of these indicators of foreign ownership participation in Chinese banks are highly correlated with bank non-performing loan ratios, indicating that foreign investment has improved prudent behaviour in Chinese banks.

We now want to test the influence of foreign strategic investment on domestic bank corporate governance and the role of corporate governance in bank prudent behaviour. We collect Chinese bank corporate governance data according to four groups: bank ownership, board composition, risk management, and CEO compensation. Bank ownership is always a hot topic in bank corporate governance. Earlier studies suggest that ownership is significantly related to a firm's financial performance (Oswald and Jahera, Jr., 1991). A higher state ownership of banks is believed to be associated with lower efficiency (LLSV, 2002; Micco, Panizza, and Yanez, 2009). Furthermore, in developing countries with weaker investor protection and legal enforcement, concentrated bank ownership can pro-

¹ All the regressions are estimated using a heteroskedasticity-consistent covariance matrix estimator and the standard errors are clustered at the bank level. Although not reported, the time-specific effects are controlled by year dummies in all the regressions.

vide high private benefits of control. Therefore, we track the state ownership of Chinese banks and the ownership concentration ratios for all of our sample banks. A sound internal corporate governance system with a reasonable board size and board composition can mitigate the potential agency problem. Earlier studies suggest that non-executive directors add value to firms by providing expert knowledge and monitoring services (Fama, 1980; Singh and Davidson, 2003). In our study, we collect both the board size and the board composition information for our sample banks. Finally, the bank risk management system and CEO compensation have raised great concerns for most of the Chinese banks and they are accordingly taken into account in our analysis as well. Altogether, we collect eleven variables referring to the Chinese bank corporate governance system. All the variables are specified by simple zero/one values and principal component analysis is applied to construct the final corporate governance indices of all the sample banks. A detailed description of the variables that are applied for the construction of the bank corporate governance and bank ownership indices is provided in Table 6 in the appendix. The information on the Chinese bank corporate governance data is manually collected from bank annual reports and the media.

We then test the direct link between bank corporate governance indices and bank risk. Table 3 presents the regression results with three proxies of corporate governance performance as independent variables and the bank non-performing loan ratio as the dependent variable. The three corporate governance proxies are: a dummy variable on whether the foreign board members are present in a certain bank, the corporate governance index built on six corporate governance variables, and the bank ownership index built on five bank ownership variables. Again, we control bank-specific and macroeconomic conditions and the standard errors are clustered at the bank level. The estimation results suggest a negative and significant relationship between bank corporate governance performance and bank non-performing loan ratios.

We finally analyse the role of corporate governance in foreign bank entry into China and test whether the bank risk-taking incentives are mitigated through better corporate governance practices. We regress the non-performing loans ratio on the three foreign investment proxies and control the two corporate governance indices in all the regressions. The results in Table 4 shows that all the foreign investment proxies are negatively correlated with the bank non-performing loan ratios. However, the significance of the relationship between foreign investments and bank risk disappears when bank corporate govern-

ance performance is controlled. The two corporate governance indices are both negatively and significantly correlated with decreased bank non-performing loan ratios. The results indicate that the adoption of a market-oriented corporate governance model has played an important role in Chinese bank performance. Actually, bank risk-taking incentives are mitigated through an improved corporate governance system.

4 An event study analysis

In the following empirical analysis instead of applying financial performance data we track the market reactions of foreign strategic investment in Chinese banks. Earlier cross-country merger and acquisition studies suggest positive gains for target and acquirer firms when the acquirer firms operating in a better institutional environment. Bris and Cabolis (2008) find that target abnormal returns increase with better shareholder protection and accounting standards in the acquirer's country for control acquisitions. Focusing on FDI flows to emerging markets, Chari et al. (2009) argue that developed market acquirer enjoy significant and positive abnormal stock returns for control acquisitions of emerging market targets.

In our study, we have collected 30 announcements on foreign strategic investments in Chinese banks from December 2001 to January 2009. Among them, 28 announcements are acquisition events and 2 announcements are sell events. For each announcement daily abnormal returns around the announcement date are estimated using market model. The market return used in the estimation is the Shanghai A share index. Until 2009, there are only 14 listed banks in China and most of the strategic investments took place before the banks go listed. Therefore, instead of estimating abnormal returns of the exact target we construct a bank index with six joint stock bank listed earlier than December 2001 and estimate the abnormal returns of this bank index for all the 30 announcements.

Cross-border bank merger and acquisitions can reduce risk through diversification; decrease the potential cost of financial distress, bankruptcy, and loss of franchise value (Berger, Demsetz, and Strahan 1999). Bank merger and acquisition also serve as a manager disciplining mechanism, replacing the existing manager with a more competent

one and improving the efficiency within the bank. The efficiency improvement perceived by investors should produce positive abnormal returns to merging firms. For the rivals, however, negative abnormal returns are expected. This is because the higher efficiency of merging firms can intensify competition in product and factor markets, resulting in competitive disadvantage for the rivals. In China, the banking sector can be classified in three groups: the big four state-owned banks, the national joint stock banks and the regional city commercial banks. Banks within each group compete with each other although the competition across the three groups is very low. The six listed joint stock banks taken in our bank index for the abnormal return estimation are strong competitors for the other joint stock banks; however they are non-competitors for the big four state-owned banks and city commercial banks. In this context, an efficiency improved acquisition event for a joint stock bank should produce a negative abnormal return for the six-joint-stock-bank index as competitors; while a positive acquisition event for a big four state-owned bank or city commercial bank should exhibit a positive abnormal return for the six-joint-stock-bank index as non-competitors.

Table 5 summarize the average cumulative abnormal returns on the six-joint-stock-bank index for all the 30 announcements on three event windows. Panel I shows that the first foreign strategic investment within the three banking groups is always a big event. As non-competitors for the joint stock banks, the cumulative abnormal returns for first acquisition event within the big four state-owned banks and the city commercial banks are highly positive and significant. As competitor for the other joint stock banks, the cumulative abnormal return for the first foreign investment on a joint stock bank is negative. Furthermore, panel II shows that the average cumulative abnormal returns for all the non-competitor acquisition events are positive and significant; while the average cumulative abnormal returns for all competitor acquisition announcements are negative. The results demonstrate a positive market reaction to the foreign strategic investments. The market believes that foreign strategic investment will improve Chinese bank performance. Panel III summarizes the average cumulative abnormal returns for the two sell event announcements. From the end of 2008 to the beginning of 2009, two of the big four state-owned banks, Bank of China and China Construction bank, suffered stake dumps from three foreign strategic investors. However, the stock abnormal returns for the six-joint-stock index didn't react significantly to these three sell events. Because of the limited ownership par-

ticipation on these two Chinese banks, the Chinese banking system was not affected severely by the strategic investors' financial crises.

5 Conclusions

Generally, foreign bank entry into developing countries affects the domestic banking markets through two mechanisms: increased bank competition and the adoption of a better corporate governance system through bank mergers and acquisitions for the domestic banks. The increased competition can both increase bank operating efficiency and decrease bank franchise values, which accordingly aggravate the bank risk-taking behaviour. However, the improved corporate governance will lead to long-term performance improvement. For this reason, many developing countries have introduced foreign strategic investors with the hope that substantial improvements in bank corporate governance will be brought to the domestic banks. While in most other countries, foreign investment took the form of direct takeovers or majority shareholding, foreign investment in China's banks has taken the form of minority shareholding with very limited ownership involvement. How much influence foreign investment will have on the domestic banks is therefore debatable.

In our empirical attempt, we first assess the direct effect of foreign participation on the prudent behaviour of the Chinese banking system, measured by bank non-performing loan ratios. We find that foreign investors tend to mitigate bank risk taking. We further identify the role of corporate governance reforms in bank performance during foreign ownership and management participation. Our empirical results suggest that foreign minority investment exerts a positive effect on bank prudent behaviour through an improved corporate governance system. In our event study analysis we find a positive market reaction to foreign strategic investment announcements. Furthermore, our event study analysis shows that due to limited ownership involvement, foreign banks have less contagion effect on Chinese banks during the financial crisis in 2008 and 2009.

Generally, we find evidence that foreign minority investors exert a positive influence on the prudent behaviour of Chinese banks through an improved corporate governance system. The way that China has opened up for foreign competition has so far been successful. However, there are still concerns about the foreign bank entry model in China.

The ownership shares of foreign strategic investors are relatively small and their management involvement is minimal. It is therefore unclear whether foreign strategic investors have sufficient incentives and opportunities to exert enough influence on Chinese banks. The problem of corporate governance and risk management in Chinese banks, to some extent, still exists however the early experience leads to believe that a more integrated financial market is likely to benefit the Chinese banking system.

Table 1

This table shows descriptive statistics for the variables in the regression analysis. *Foreign Inv.* is the dummy variable of whether the bank has a foreign strategic investor, *Foreign Total* is the percentage of foreign strategic investments, *Total10* is the dummy variable of whether the foreign strategic investor has a stake of more than 10 percent, *Foreign Board* is the dummy variable on whether there is a foreign investor nominated board member in the bank's management board, *CG* is the bank corporate governance index built on six selected corporate governance variables, *OwnCG* is the bank ownership index built on five selected bank ownership variables, *LogTA* is the natural logarithm of a bank's total asset, *Equity* is a bank's total equity, *GDP* is the annual gross domestic product, *CPI* is the annual consumer price index.

Variables	Mean	Std.Dev	Min	Max	N
Panel I: Foreign Strategic Investment					
Foreign Inv.	0.53	0.50	0	1	123
Foreign Total	6.92	9.03	0	26.42	123
Total10	0.11	0.32	0	1	126
Panel II: Bank Corporate Governance Performance					
Foreign Board	0.50	0.50	0	1	123
CG	4	1	1.49	4.95	122
OwnCG	4	1	1.57	5.31	122
Panel III: Banking System and Macroeconomic Variables					
Log(TA)	5.43	0.80	3.63	6.94	123
Equityratio	0.05	0.03	0	0.313	117
GDP Growth	10.48	0.98	7.10	11.40	126
CPI	103.22	2.10	99.20	106.50	120

Table 2

This table shows the impact of foreign strategic investment on Chinese bank overall performance. The dependent variables are bank non-performing loan ratios and bank return on total assets. The results are estimated from OLS regressions with standard errors clustered at the bank level, where ** denotes significance on the 1%-level, * on the 5%-level, † on the 10%-level. The bank-specific and time specific effects are controlled in all the regressions. Foreign Inv. is the dummy variable of whether the bank has a foreign strategic investor, Foreign Total is the percentage of foreign strategic investments, Total10 is the dummy variable of whether the foreign strategic investor has a stake of more than 10 percent.

	NPL	NPL	NPL
Foreign Inv	-4.835 † (2.452)		
Foreign Total		-0.212* (0.096)	
Total10			-2.971 † (1.612)
GDP Growth	-3.143** (1.058)	-3.336** (1.009)	-3.770** (1.122)
CPI	0.473 (0.296)	0.396 (0.305)	0.417 (0.402)
Log(TA)	3.415 † (1.745)	2.760 † (1.568)	2.335 (1.614)
Equityratio	16.647 (21.148)	11.574 (19.633)	1.632 (23.554)
Constant	-27.959 (37.270)	-14.887 (34.990)	-11.052 (42.518)
R-squared	0.301	0.270	0.204
N	110	110	110

Table 3

This table shows the impact of corporate governance on Chinese bank risk taking. The dependent variables are bank non-performing loan ratios. The results are estimated from OLS regressions with standard errors clustered at the bank level, where ** denotes significance on the 1%-level, * on the 5%-level, † on the 10%-level. The bank-specific and time specific effects are controlled in all the regressions.

	NPL	NPL	NPL
Foreign Board	-3.705 † (1.869)		
CG		-2.779* (1.137)	
OwnCG			-2.703* (1.211)
GDP growth	-3.174** (0.994)	-2.623 † (1.442)	-3.041** (1.090)
CPI	0.357 (0.225)	0.417 (0.419)	0.340 (0.331)
Log(TA)	1.667* (0.675)	1.265* (0.539)	0.749 (0.620)
Equityratio	-0.011 (0.018)	-0.011 (0.017)	-0.016 (0.018)
Constant	2.284 (24.235)	-0.013 (33.982)	12.901 (29.225)
R-squared	0.395	0.461	0.437
N	110	109	109

Table 4

This table shows the impact of foreign strategic investment on Chinese bank risk taking controlling bank corporate governance performance. The dependent variables are bank non-performing loan ratios. The results are estimated from OLS regressions with standard errors clustered at the bank level, where ** denotes significance on the 1%-level, * on the 5%-level, † on the 10%-level. The bank-specific and time specific effects are controlled in all the regressions.

NPL					
Foreign Inv	-2.933 (1.750)			-1.763 (2.058)	
Foreign Total		-0.056 (0.069)			-0.004 (0.081)
Total			-1.316 (1.384)		
CG	-2.834* (1.140)	-3.062* (1.415)	-3.267* (1.345)		
OwnCG				-2.856* (1.249)	-3.302* (1.451)
GDP Growth	-2.291 (1.478)	-2.479 (1.561)	-2.51 (1.608)	-2.822* (1.124)	-2.940* (1.167)
CPI	0.570 (0.377)	0.527 (0.445)	0.550 (0.483)	0.428 (0.299)	0.396 (0.364)
Log(TA)	2.815* (1.161)	2.234* (1.068)	2.135 † (1.083)	1.238 (1.195)	0.601 (0.977)
Equityratio	10.709 (18.098)	4.419 (18.439)	1.703 (17.908)	-4.930 (18.846)	-11.962 (21.942)
Constant	-32.892 (32.609)	-23.060 (38.321)	-23.962 (41.508)	-3.630 (30.147)	5.810 (33.709)
R-squared	0.434	0.400	0.399	0.415	0.404
N	109	109	109	109	109

Table 5

This table shows the average cumulative abnormal returns on the six-joint-stock-bank index for all the 30 buy and sell announcements on three event windows.

	Event Group	Number of Events	Event Window	
			(-1,1)	(0,2)
Panel I				
	First City Commercial	1	2.23***	2.13
	First Big Bank	1	2.92**	0.82
	First Joint Stock	1	-2.96	-1.26
Panel II				
	Non Competitor	18	0.79**	0.62**
	Competitor	10	-0.60	-0.13
Panel III				
	Sell event	2	-0.19	-0.17

Appendix

Appendix - Table 6

This table contains all questions we used for the construction of bank ownership index and corporate governance index. Questions could either be answered with yes or no. We specify these answers as zero/one values and the index was then constructed by running a principal component analysis.

Relevant questions for the construction of ownership index
1. Does the state own more than 50 percent of the bank?
2. Does the bank have foreign strategic shareholders?
3. Do foreign strategic shareholders have a share of more than 10 percent?
4. Is the ownership concentration ratio of the largest shareholder greater than 50 percent?
5. Is the ownership concentration ratio of the first three shareholders greater than 50 percent?
Relevant questions for the construction of corporate governance index
1. Is there independent board member in the bank's management board?
2. Do the independent board members account for more than 30 percent of the total management board?
3. Is there foreign shareholder assigned board member in the bank's management board?
4. Is there foreign executive board member in the bank's management board?
5. Is there independent risk management committee in the bank?
6. Is there disclosed performance related CEO compensation package in the bank?

Appendix - Table 7

This table shows the transition of bank corporate governance model in China.

Control based CG Model	Market Oriented CG Model
1. Bank Ownership	
a) State as single or majority shareholder	a) Reduced state ownership
b) highly concentrated bank ownership	b) diversified bank ownership
2. Board Composition	
a) Small board size without non-executive board members	a) improved board size with non-executive board members
b) Without independent board member	b) With independent board member
3. Bank Risk Management	
a) Without independent risk management committee	a) With independent risk management committee
4. CEO Compensation	
a) no performance related CEO compensation	a) performance related CEO compensation

Appendix - Table 8

This table shows the summary of banks partially acquired by foreign investors.

Chinese banks	Foreign Investor	Percentage	Year
Bank of Beijing	ING Bank N.V.	19.9	2005
	IFC	5.00	2005
Bank of China	RBS China Investments S.A.R.L.	10.00	2005
	Asia Financial Holding Pte. Ltd.	5.00	2005
	UBS AG	1.61	2005
	Asian Development Bank	0.24	2005
Bank of Communication	HSBC	19.9	2004
Bank of Nanjing	BNP Paribas	19.20	2005
	IFC	5.00	2001
Bank of Shanghai	HSBC	8.00	2001
	IFC	7.00	2001
	Shanghai Commercial bank	3.00	2001
China Bohai Bank	Standard Chartered Bank	19.9	2005
China Citic Bank	BBVA	5.00	2006
China Construction Bank	Bank of American	9.00	2005
	Asia Financial Holding Pte. Ltd.	5.10	2005
China Industrial Bank	Hang Seng Bank	15.98	2004
	GIC Special Investments	5.00	2004
	IFC	4.00	2004
China Industrial and Commercial Bank	Goldman Sachs	5.75	2006
	Allianz	2.25	2006
	American Express	0.44	2006
Guangdong Development Bank	Citi Bank leded Consortium	85.59	2006
Hangzhou City Commercial Bank	Common Wealth Bank of Australia	19.90	2005
Hangzhou City Commercial Bank	Asia Development Bank	4.99	2006
Huaxia Bank	Deutsche Bank	7.02	2005
	Sal Oppenheim	4.08	2005
	Deutsche Bank Luxemburg	2.88	2005
Jinan City Commercial Bank	Common Wealth Bank of Australia	11.00	2004
Minsheng Bank	Asia Financial Holding	4.55	2004
	IFC	1.08	2004
Ningbo City Commercial Bank	OCBC (Singapore)	12.20	2006
Shanghai Pudong development Bank	Citigroup	5.00	2003
Shenzhen development Bank	New Bridge Capital	17.89	2004
Tianjing City Commercial Bank	Australia and New Zealand Banking Group Ltd.	20.00	2005
Xian City Commercial Bank	IFC	2.50	2002
	Scotiabank	2.50	2002

Appendix - Table 9

This table shows the cumulative abnormal returns of the buy and sell events.

Date	Chinese bank	Foreign Investor	Percent	Cumulated Abnormal Returns						
				(-1,1)		(0, 2)		(-1,2)		
				Bank	Industry	Bank	Industry	Bank	Industry	
Panel I Joint Stock Bank										
Bank and Competitor Abnormal Returns										
31Dec 2002	SH Pudong Development Bank	Citi bank	5.00	1.68	-2.96	-1.66	-1.26	1.62	-2.56	
23Otc 2003	China Minsheng Bank	IFC	1.08	1.49 **	0.82	3.09 ***	0.51	3.69 ***	0.83	
28May 2004	Shenzhen Development Bank	New Bridge Capital	17.89	6.02 **	-1.05	3.33	-0.13	4.55 **	-1.29	
15Otc 2004	China Minsheng bank	Asia Financial Holding	4.55	2.38	0.94	-1.94	-1.25	1.99	1.01	
17Otc 2005	Huaxia Bank	Deutsche bank, Sal. Oppenheim	14	2.86 **	-1.28	3.00 *	0.30	3.90 *	-0.18	
03Jun 2008	China Citic bank	BBVA	10.07	1.24 **	-0.66	0.76	0.67	2.03 ***	0.09	
Competitor Abnormal Returns										
17Dec 2003	China Industrial Bank	Hang Seng Bank, GIC, IFC	24.98		-0.42		2.03 **		1.30	
06Sep 2005	China Bohai Bank	Standard Chartered Bank	19.90		-1.44 ***		0.96		-0.08	
16Nov 2006	Guangdong Development Bank	Citi Bank leaded Consortium	85.59		-1.12		0.70		0.98	
23Nov 2006	China citic bank	BBVA	5		1.19		-3.85 ***		-1.42	
Panel II City Commercial Bank										
28Dec 2001	Bank of Shanghai	HSBC, IFC, SH. Commercial Bank	18.00		2.23 ***		2.13		1.42	
30Aug 2002	Xian City Commercial Bank	Scotia Bank and IFC	5.00		-0.41		1.70		1.35	
08Sep 2004	Jinan City Commercial Bank	Common Wealth Bank of Australia	11		1.85 ***		0.91 **		1.96 ***	
25Mar 2005	Bank of Beijing	ING, IFC	24.9		0.17		0.85		0.70	
20Apr 2005	Bank of Hangzhou	Common Wealth Bank of Australia	19.9		1.63 **		0.79		1.93	
23Sep 2005	Bank of Nanjing	BNP	19.2		-0.90		-0.43		-0.74	
01Dec 2005	Tianjing City Commercial Bank	ANZB	20		2.03 **		0.69		2.39 ***	
28Aug 2006	Bank of Hangzhou	Asia development bank	4.99		-1.23		-0.30		-1.44	
Panel III Big Bank										
17Jun 2005	China Construction Bank	Bank of America	9.00		2.92 **		0.82		2.60 ***	
01Jul 2005	China Construction Bank	Asia Financial Holding	5.10		2.39 **		1.62 *		2.56 **	
18Aug 2005	Bank of China	RBS	10.00		0.62		1.47 ***		1.06	
31Aug 2005	Bank of China	Asia financial holding	10.00		-0.19		-1.01		-0.47	
06Aug 2004	Bank of Communication	HSBC	19.9		0.93		2.57		1.86 *	
27Sep 2005	Bank of China	UBS	1.61		0.85 ***		0.07		0.36	
10Otc 2005	Bank of China	Asia development bank	0.24		1.29		0.87		1.21	
27Jan 2006	China Indus. and Comm. Bank	Goldman sachs, Allianz, AE	8.74		1.21		-0.51		-0.24	
27May 2008	China Construction Bank	Bank of America	1.75		1.10		0.15		-0.87	
18Nov 2008	China Construction Bank	Bank of America	8.38		-2.36		-1.31		-2.42	
Panel IV Sell Events										
31Dec 2008	Bank of China	UBS	1.33		0.25		0.54		1.20	
07Jan 2009	Bank of China, Bank of Const.	RBS, Bank of America	4.26		-0.62		-0.87		0.06	

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