Banking practices in China, much like business practices, can be very different compared to what treasurers and cash managers are accustomed to in other markets, such as the United States, Canada or Europe. For any company looking to do business in China, understanding the differences and nuances of banking in China can help your treasury team better manage your banking structure. For companies that are new entrants or looking to enter the China market, understanding these nuances is important and is recommended as part of a company’s due diligence of China market entry.

1 LOCAL BANKING STRUCTURE IN CHINA

In China, there is one central bank (People’s Bank of China), three policy banks (China Development Bank, The Export-Import Bank of China, Agricultural Development Bank of China), five state-owned commercial banks (also called the “big five” banks, which are Agricultural Bank of China, Bank of China, Bank of Communications, China Construction Bank, Industrial & Commercial Bank of China), and 12 joint-stock commercial banks, city commercial banks, rural commercial banks, foreign banks, etc.

Local banks’ hierarchy in China is structured in the following tiers (from low to high):

Sub-branches (equivalent to a branch in the United States) are managed by the branch (equivalent to the bank regional offices in the U.S.) at either the city and/or provincial level, followed by headquarters.

What’s different compared to the United States is the decentralized nature of banking operations.
What’s different compared to the United States is the decentralized nature of banking operations. As each sub-branch has their own relationship team, operations and customer service group (i.e., not centralized), the expertise and the customer experience of each sub-branch may not be consistent even for the same bank.

Additionally, the implementation of certain banking regulations and/or bank policies may differ between regions, leading to scenarios where certain services can be offered in certain regions’ branches and not in others. Therefore, companies wishing to develop local banking relationships should evaluate the bank’s suitability based on the specific branch’s expertise and service capability, in addition to the bank’s overall capability.

2 RMB ACCOUNT TYPES

There are various types of accounts in China with which companies should be familiar. The common account types that companies utilize are:

- **Basic Account** — Allows for cash deposits, withdrawals and payments, including salary payments. A company can only have one basic account overall due to People's Bank of China (PBOC) regulations. This is the only account type from which cash can be withdrawn.

- **General Account** — Allows for payments and cash deposits, though cash cannot be withdrawn from a general account. There is no limitation on the number of general accounts that a company can have.

- **Specialized Account** — Opened for a designated purpose, such as project funds, capital expenditures, overseas borrowing, intercompany lending or borrowing, etc.

- **Capital Contribution Account** — Allows registered capital for a company to be contributed in the RMB currency.

3 CURRENT ACCOUNT vs. CAPITAL ACCOUNT TRANSACTIONS

**Current account transactions** are related to imports and exports of goods and services and income from abroad, as well as current transfers (such as donations). Trade transactions would be the classic example of a current account transaction, which is delineated further into service and goods trade. Dividend repatriation would also be considered a current account transaction.

**Capital account transactions** are those that would affect the capital base of a company within China. For example, when a company establishes an entity in China, it must determine the “registered capital,” which is the amount of capital from overseas that would be invested into the entity. Any initial injection of or subsequent changes in registered capital, or cross-border M&A using the company’s capital, are considered capital account transactions.

For companies operating or thinking about establishing in China, it’s important to be aware of the differences on how current account and capital account transactions operate, as such operational differences do not exist in many markets such as the U.S., Canada and Europe. When dealing with capital account transactions, the inflow and outflow of these transactions are restricted and only processed when the appropriate verifications and procedures are carried out.

While the current account is “open,” companies should ensure that transactions are bona fide and supported by robust documentation. This is especially the case for dividend repatriation where, even though it’s classified as current account transaction, the process and procedure can be cumbersome depending on the market condition.
4 **NON-RESIDENT ACCOUNTS**

There are three types of non-resident accounts in China: OSA (offshore account, which is not available for RMB), NRA (called “non-resident account” though it is a type of non-resident account) and FTA (free trade account).

Non-resident accounts (NRAs) can be set up by foreign companies as well as Chinese companies’ subsidiaries overseas. For Chinese companies with overseas subsidiaries, NRAs can help provide a linkage to onshore and offshore entities and related resources. Non-resident accounts are available in RMB and foreign currencies, including USD.

In addition to non-resident accounts, companies may also consider multicurrency accounts offered in their home country that provide many similar benefits. For example, PNC offers multicurrency accounts in the RMB currency for clients who wish to conduct payments in RMB with their trading partners while providing the features and benefits of a U.S.-based account that’s integrated with PINACLE®, PNC’s top-rated corporate online and mobile banking portal.

5 **DOCUMENTATION REQUIREMENT FOR CROSS-BORDER PAYMENTS**

Unlike in the United States, where cross-border payments can be initiated without submitting supporting documents to the bank, banks in China generally require China-based companies to provide supporting documentation to verify a cross-border payment’s authenticity. This is the result of regulatory requirements where cross-border transactions are not fully open and therefore require verification by the banks.

For current account transactions, companies conducting goods-trade and service-trade would be required to submit documents relevant to the trade transactions for review. Dividend repatriation is also a type of current account transaction requiring a specific process and procedure.

For capital account transactions, documents vary depending on the type of capital transaction. Types of transactions include registered capital contribution or reduction, intercompany borrowing and lending, and overseas M&A.

The required information may differ depending on market and regulatory conditions, local practices where the bank is located, the bank’s own requirements, and even the payment amount.

Domestic payments within China (i.e., China-to-China) typically do not require supporting documentation.

For companies operating or thinking about establishing in China, it’s important to be aware of the differences on how current account and capital account transactions operate.
LOCAL PAYMENT INSTRUMENTS AND PAYMENT PRACTICES
While many payment practices are not unlike those in the U.S. market, companies operating in China should be familiar with some of the local payment practices, such as the use of CNAPS (China National Advanced Payment System) and paper-based instruments such as checks, credit vouchers, bank commercial drafts, etc.

Bank commercial drafts do not have a direct U.S. equivalent. Commercial drafts are often used for business-to-business payments and have a supply chain finance feature: Invoices are considered paid when commercial drafts are received by the payee, though funds do not settle until the payment date on the draft, which can be up to six months for paper-based acceptance drafts and 12 months for electronic bank drafts. Even though the maturity date can be quite long, commercial drafts may also be discounted prior to maturity.

As commercial drafts are a popular payment instrument in China, and oftentimes would be the payment vehicle of choice for certain clients, understanding these drafts and how they could impact a company’s sales strategy and cash conversion cycle is important, alongside other available payment channels.

ONSHORE AND OFFSHORE RMB MARKETS
There are two currency markets for the RMB: the onshore RMB market and the offshore RMB market. The onshore RMB market refers to RMB traded and transacted in mainland China (excluding Hong Kong, Macau and Taiwan), while offshore RMB refers to all markets outside of mainland China, the most active of which is Hong Kong. Other notable offshore RMB centers include London and Singapore.

The onshore RMB (CNY) market has a managed foreign exchange rate (discussed further below under central parity rate) and its own interest rates market. Companies within the onshore environment can conduct foreign exchange transactions and cross-border payments in the RMB in a managed environment, where current account transactions are relatively open and capital transactions are more scrutinized.

The offshore RMB (CNH) market has a free-floating foreign exchange rate and its own interest rates market, and could therefore have differing rates than the onshore market. Foreign exchange and cross-border payments in RMB can be conducted freely without restriction.

PNC’s RMB multicurrency account would be considered in the offshore market, where clients’ RMB can be freely traded and transacted without restriction.

CENTRAL PARITY RATE
The central parity rate is the RMB foreign exchange reference rate in the onshore RMB market set by the People’s Bank of China (PBOC) on a daily basis. The onshore market foreign exchange rate is allowed to float plus or minus 2% from the central parity rate (the FX trading band).

While the offshore RMB is freely floated and does not use the central parity rate, offshore and onshore RMB rates generally track closely with each other, though rate differences can exist, especially during periods of market volatility.

On August 11, 2015, the PBOC announced its exchange rate “reform,” whereby the PBOC sets the central parity rate relative to the USD for the day based on the previous day’s closing rate, market supply and demand, as well as the valuation of other major currencies.
On May 26, 2017, China’s Foreign Exchange Trade System (CFETS) announced the introduction of a counter-cyclical factor to the existing pricing model of RMB’s central parity rate against the U.S. to moderate the fluctuations driven by irrational sentiment in the foreign exchange market.

**FREQUENT AND SUDDEN CHANGES IN BANKING REGULATIONS**
Banking regulations in China can change on a dime and are often opaque. As a result, companies may find that regulation changes may cause certain banking transactions and services to be restricted or more closely scrutinized.

Companies should stay abreast of the banking regulatory changes in China and remain nimble in the event regulatory changes impact the services banks can offer.

**DEVELOPMENT OF FINTECH**
Fintech development has been prolific in China so that many transactional activities that were historically done through banks are now possible entirely outside of the banking channel. For P2P and C2B payments, the likes of WeChat Wallet (developed by Tencent) and Alipay (by Alibaba) have changed people’s behavior such that individuals no longer need to carry a wallet or credit cards: Payments can be instantly transacted over the phone via QR codes, which are now ubiquitous in China. Individuals can deposit balances at internet finance companies through a click on their smartphone, sometimes offering higher yield than traditional banks. Individual and small-business financing through P2P platforms or internet finance companies are also now commonplace, cutting into banks’ core business.

For foreign companies based in China with sales to consumers, in addition to leveraging traditional banking channels for sales, companies now need to have strategies in leveraging these fintech payment channels to reach their customers. Whether or not fintech will expand into B2B payments and the traditional corporate banking space remains to be seen.

**ABOUT THE AUTHOR**
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Chris Chen has extensive domestic and international cash management experience through his work with PNC’s Treasury Management group. He has a bachelor’s degree in economics and music from the Schreyer Honors College, Pennsylvania State University. Born in Taiwan, Chen is fluent in English and Mandarin.

Banks and Fintech: China’s Financial Environment Now

China’s financial environment has experienced significant changes over the last few years, and we expect the trend to continue. PNC’s Shanghai Representative Office can provide overall guidance and help you understand the implications of conducting business in China.

For more information, please contact your PNC Relationship Manager or visit pnc.com/GoChina.