

Payment Service Industry in China: 29 Jul 05

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Banking Sector Overview

China's accession to WTO marked a new era for its financial service sector. With a population of 1.3 billion, China is a huge and lucrative market for payment services. It is one of the biggest card issuers globally with more than 800 million bankcards, and has a nation-wide POS and ATM infrastructure.

Among the state-owned commercial banks in China, the top five banks, in that order, are Industrial and Commercial Bank of China (ICBC), Bank of China (BOC), China Construction Bank (CCB), Agricultural Bank of China (ABC), and Bank of Communications (BoCom). The "Big-Four" banks dominate the market with more than 140,000 branches and 30,000 ATMs together nationwide, and control about 54% in total banking assets. There are other more than 100 smaller national and city commercial banks and credit cooperatives.

At present, no single foreign investor can acquire more than 20% in a local financial institution in China. The upper limit of total foreign shareholding is capped at 25%. Temasek Holdings, HSBC and Bank of America have minority stakes in China Minsheng Bank/CCB, BoCom and CCB respectively. The regulators encouraged the commercial banks to forge partnership with overseas investors, with the objective to push the state-owned banks to establish and comply with the international corporate governance and risk management standards, and to bring greater transparency.

Supervisory Agencies

The two major supervisory agencies for the Chinese banking sector are People's Bank of China (PBOC) and China Banking Regulatory Commission (CBRC).

PBOC was established in Dec 1948, and was designated to perform the role of a central bank by the National People's Congress in Mar 1995. In Mar 2003, the supervisory functions for the financial sector were taken out and transferred to a new entity, CBRC. PBC as a central bank will play a more focused macro-economic management role in formulating and implementing monetary policies, supervising and managing the financial risk, and safeguarding the financial stability of the banking sector.

For CBRC, its key role is to promote the financial stability and develop innovative products and services in the banking sector.

Payment Cards Environment

China's first bankcard was issued in 1985. Its card market is still in its initial development stage. Credit card segment is insignificant compared to debit cards. By end 2004, more than 815 million bankcards have been issued by about 150 financial institutions. Debit cards accounts for more than 95% of the card base.

Under the WTO terms, foreign banks are not allowed to issue RMB-denominated credit cards until 2007. Credit card is a lucrative business opportunity for foreign banks and credit card operators. Currently foreign banks have strategic partnership with local banks for credit card issuance. The deregulation in 2007 will lead to greater competition in the retail banking space. Credit card market is expected to grow significantly with the change in consumer attitudes, foreign banks' innovative products and the greater accessibility of credit card in major cities supporting the 2008 Olympic Game in Beijing and 2010 World Expo in Shanghai.

The national card standard, "China Financial IC Card Specification" was first published by PBOC in 1997. All bankcards supplied by the card vendors and distributed by the commercial banks now must comply with this card specification.

Growth in Card Usage

The total bankcard transaction value grew significantly from RMB18 trillion in 2003 to RMB 27 trillion in 2004 while transaction totaling 5.1 Billion last year. The card transaction value in 2004 accounts for 5% of total retail consumption, compared to 2.1% in 2001. This is relatively low compared to developed countries.

The banking-related government agencies, including PBOC and CBRC, expected the usage targets by 2008 as:

- 60% of merchants acquired for establishments with annual turnover exceeding RMB 1 Million;
- 30% of total retail consumption in major cities.

Payment Terminal Infrastructure

Since 1990, with the launch of the Golden Card projects, domestic banks developed their own infrastructure and payment networks. Different standards and technologies were adopted. In mid 1990, PBOC wanted to unify the fragmented infrastructure and work closely with the domestic banks to set up a single bankcard network. In 2002, China UnionPay (CUP) was officially formed. To date majority of the POS terminals & ATM are connected to the CUP network. The foreign banks are not included neither as shareholders or participating banks at present.

The bankcards are now widely accepted at more than 500,000 terminals in 340,000 establishments in China.

Local POS suppliers, including Fujian Start Computer Equipment Co Ltd, PAX Technology Ltd, Fujian Newland Computer Co Ltd, etc account for majority of the POS terminals deployed in China.

The first ATM was installed by BOC in 1988. At present, the ATMs are mainly owned by the banks with the "Big Four" together deploying more than 60% of all ATMs. A wholly-owned subsidiary of CUP, named China UnionPay Tonghui, was incorporated in May 2005 to explore the feasibility of operating its own ATMs.

CUP's first foray into overseas market commenced in Jan 2005 with its connection extended to Korea, Singapore and Thailand for POS and ATM services. It has positioned itself as a "global card association" competing with MasterCard and Visa globally.

It further expanded its international footprint with the signing of partnership agreements with three overseas service providers in May 2005 including Discovery Financial Services in US, SMCC in Japan and EUFISERV in Europe. These partnerships will offer connectivity to more than 7 million merchants and cash access points in 14 countries.

Internet and Mobile Payment

These new payment channels have not taken off in China. Shanghai Huateng Software Systems Co Ltd pioneered Internet payment since early 2000. The company's electronic payment service was later acquired by CUP in 2002 and renamed Chinapay E-payment Services Co Ltd. There are several online and mobile payment operators mainly in major cities including Beijing, Shanghai and Guangzhou.

In China, the Internet penetration rate remains very low at less than 10%.

Future Directions

China's WTO membership changed the way financial institutions conducting the businesses. The domestic financial institutions and payment service providers have to strengthen their core capabilities and enhance the competitive edge. This will enable them to face the challenges of international operators when China's WTO commitment of opening up the financial sector comes into place in 2007.

The writer was the General Manager of NETS Singapore and currently the CEO of an IT company in China. He has extensive business development experience in the payment industries in Singapore and the region. This article is contributed in his personal capacity.