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First US approval for Chinese bank purchase

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Industrial & Commercial Bank of China has gained US approval to purchase an American bank, marking a watershed moment for Chinese lenders looking to gain a foothold in the US.

ICBC's purchase of the US subsidiary of Hong Kong's Bank of East Asia comes after months of frustration for the Chinese acquirer as the proposed acquisition was scrutinised by US authorities.

It marks the first time the Federal Reserve has allowed a Chinese institution to buy an American bank and industry lawyers said it would spur dealmaking by Chinese institutions, among the biggest banks in the world by market capitalisation.

The approval follows the US-China Economic Dialogue last week where US officials promised to deliver a response to the applications "expeditiously" and noted they were "encouraged" by a positive review of Chinese banking supervision by the International Monetary Fund and World Bank.

Chinese officials had pressed the Fed for the decision, which marks the first time the US central bank has recognised Chinese regulation of banks as meeting a standard of "comprehensive, consolidated supervision".

The communique following the dialogue, attended by Tim Geithner, Treasury secretary, was a "slam dunk", said Ernie Patrikis, a partner at White & Case who acted for ICBC. The Chinese bank agreed more than a year ago to buy 80 per cent of Bank of East Asia's US subsidiary, which has just $780m in assets. It has already acquired a stake of that size in the Hong Kong bank's Canadian unit.

ICBC, the largest bank in China with $2.5tn in assets, is 70.7 per cent-owned by the Chinese government and the move is likely to be controversial in some quarters in the US.

“Is ICBC coming in as a commercial bank or as a bank representing Chinese interests? That is a legitimate concern,” said Eswar Prasad, a professor at Cornell University and the former head of the IMF’s China division. He said the communique “reeks of quid pro quo”, with US financial groups likely to enjoy better access to Chinese markets.

The Financial Services Forum, the association for the largest US financial groups, said it had “been urging expanded participation in China’s financial [sector] as well” and touted progress on “the easing of caps on investment in Chinese securities firms”.

The Fed said that Wednesday’s decision was “specific to ICBC” but industry lawyers said it was a clear sign that the Fed was likely to approve acquisitions by other Chinese banks and future acquisitions by ICBC. Mr Patrikis predicted more acquisitions but said Chinese banks would “proceed at a logical, thoughtful pace”.

Lawyers at Sullivan & Cromwell wrote in a note to clients: “The order should create the opportunity for other leading Chinese banks to acquire US banks of a relatively modest size.”

In giving its approval, the Fed sought to minimise previous criticisms levied against Chinese banks and their national regulators. For instance, it dismissed concerns over the quality of Chinese regulation by pointing to co-operation agreements between the Fed and its counterparts in China and the continued monitoring of the health of Chinese banks by their regulators.

In its finding, the Fed said that China’s largest banks use the world’s biggest accounting firms and that “there is no evidence that Chinese accounting methods or practices at the large Chinese banks, such as ICBC, are unreliable”.

The Fed conducted discussions with the China Banking Regulatory Commission before the determination and said it “intends to further its relationship with Chinese supervisory authorities and continue to develop its understanding of Chinese banking matters”.

The US central bank previously blocked an attempted acquisition by China Minsheng, a Chinese bank, of UCB, a San Francisco-based lender that was ultimately closed by the Federal Deposit Insurance Corp. The bank was seized by the FDIC at a cost of more than $1bn to the industry’s insurance fund.

The acquisition by ICBC comes as Goldman Sachs has been reducing its equity stake in the bank. Volatile trading in ICBC's stock has been producing significant swings in Goldman's earnings.