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Chinese Banks Get Nod In U.S.

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Giant banks owned by the Chinese government are coming to the U.S.

The Federal Reserve on Wednesday approved plans by three state-backed Chinese banks to expand in the U.S., including the first acquisition of a U.S. retail-banking network by a state-owned Chinese lender.

The Federal Reserve approved the U.S. expansion plans of China's largest state-backed banks. The WSJ's Jake Lee speaks with reporter Lingling Wei.

The approval is a landmark step for U.S. banking regulators. Chinese banks long have sought access to the U.S. banking system in order to provide financing to Chinese companies operating overseas and to do business with foreign investors looking for exposure to the Chinese currency, the yuan. But they have been stymied in previous attempts by assorted delays and rejections.

"It's a significant milestone for China and the Chinese banks, which will allow them to engage in further business in the U.S. and Europe as well," said Chris Daniel, a banking lawyer at Paul Hastings LLP in Atlanta, referring to the possible influence of the Fed action on other global regulators.

The Federal Reserve effectively is giving its seal of approval to China's bank-regulatory system, a big step for U.S. regulators given their past concerns about the adequacy of Chinese supervision of banks.

The decision could open the door to other Chinese takeovers of U.S. banks, although it is unlikely China will make significant inroads into the U.S. banking industry anytime soon.

Secretary of State Hillary Clinton and Treasury Secretary Timothy Geithner met last week with Chinese counterparts for broad strategic and economic dialogue. Fed Chairman Ben Bernanke traveled with U.S. officials to China.

A statement put out by U.S. and Chinese officials after the meeting said the U.S. would "act expeditiously" on pending bank applications.

The approval comes as China, prodded by the U.S., is slowly opening its markets to foreign companies and investors.

In last week's talks, China agreed to allow foreign firms to own significantly larger stakes, although minority ones, in Chinese brokerage firms. It was a long-awaited breakthrough in a sector where restrictions have limited foreign firms.

In the largest of the approvals granted on Wednesday, the Fed gave the nod to Industrial & Commercial Bank of China Ltd., 1398.HK -0.20%one of the world's largest banking companies, to buy an 80% stake in the U.S. subsidiary of Bank of East Asia, 0023.HK 0.00%a Hong Kong company that has 13 branches in New York and California. The companies announced the deal in January 2011, but it needed regulatory approval.

The Fed also granted approval to Agricultural Bank of China Ltd. to build a branch in New York City, and to Bank of China Ltd. to build a branch in Chicago. Both are based in Beijing. Bank of China already has two branches in New York and one in Los Angeles.

ICBC, also based in Beijing, is 70% owned by the Chinese government. It is China's largest bank, with $2.5 trillion in assets, compared with $2.3 trillion in assets for the largest U.S. bank, J.P. Morgan Chase JPM +0.25%& Co. ICBC is seeking to more than double the share of profits coming from overseas operations in the next five years, to 10%, from the current 4%.

One way ICBC could distinguish itself from other banks operating in the U.S. is to offer U.S. customers access to yuan-denominated deposits. ICBC already has a branch in New York that focuses on commercial lending. The Fed took nearly two years to approve that branch, which it did in 2008.

Before approving any acquisitions of U.S. banks by foreign ones, the Fed is required by law to certify that the foreign banks are adequately supervised in their home countries. During the financial crisis, U.S. regulators rejected a bid by China Minsheng Banking Corp., a midsize lender, to buy San Francisco lender UCBH Holdings Inc., the holding company for United Commercial Bank. People familiar with the bid said U.S. regulators rejected it because of worries about Minsheng's overall strength, risk-management and anti-money-laundering procedures.

The ICBC deal marks the first Fed certification for an acquisition by a Chinese bank and for the China Banking Regulatory Commission.

"This is clearly a precedential decision," said H. Rodgin Cohen, a bank lawyer at Sullivan & Cromwell, which represented the Bank of East Asia in the transaction.

He said the Fed's nod to the Chinese regulatory system indicates that the agency would "presumably permit other at least modest transactions to occur."

In the months prior to the approval, the Fed sent teams of bank supervisors, analysts and lawyers to China to meet with regulators and banks.

Ernie Patrikis, a lawyer with White & Case, which represented ICBC, said the bank's plans for the U.S. were to "go slow and learn the market."

The Bank of East Asia is small, with $780 million in assets, and it focuses on retail and middle-market business loans. Even though ICBC has the resources to make a big splash in the U.S., Mr. Patrikis said, it would be "careful, cautious, prudent." He said other Chinese banks seemed likely to follow ICBC's lead.

The Fed made an oblique reference to national-security concerns in its order approving the transaction. It said in a footnote that some commenters had raised national security objections.

The Fed said other U.S. agencies had the authority to review national-security issues in bank-merger applications. It didn't say what other agencies looked at the application.

The Fed's approval came 13 months after ICBC's application. That is far longer than the 60 days the Fed typically takes to decide on mergers, mainly because the U.S. central bank conducted an investigation into China's regulatory practices to determine if they were up to global standards.

One reason it will be hard for Chinese lenders to make significant inroads in the U.S. is that big U.S. players like Bank of America Corp., J.P. Morgan Chase and Wells Fargo & Co. have such a commanding presence. Also, the Fed is wary of very large bank deals after the financial crisis, which exposed the risks posed by giant banks with many ties to one another.

Some U.S. banks, for their part, have been shedding their stakes in Chinese firms. The moves aren't seen as repudiations of China, but as efforts to cash in profits at a time when U.S. firms are hungry for capital.

Citigroup Inc., for example, booked a $349 million profit on the March sale of its 2.71% stake in Shanghai Pudong Development Bank. Bank of America last year recognized a $5 billion gain on sales of shares in China Construction Bank Corp.

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