Guidelines on the Measurement of Regulatory Capital of Specialized Loans of Commercial Banks

(September 18, 2008)

Article 1 For purposes of regulating the measurement of regulatory capital of specialized loans, and strengthening the risk management of specialized loans, these Guidelines are formulated according to the Banking Supervision Law of the People’s Republic of China, the Law of the People’s Bank of China on Commercial Banks and other laws and regulations.

Article 2 These Guidelines shall be applicable to the new capital accord banks determined by the Guiding Opinions concerning the Implementation of the New Capital Accord by China Banking Industry and other commercial banks voluntarily implementing the new capital accord.

Article 3 To implement the new capital accord, commercial banks shall measure the regulatory capital requirements of specialized loans according to the requirements of these Guidelines.

Article 4 The term “specialized loans” as mentioned in these Guidelines refers to the risk exposures as determined under the Classification Guidelines on the Credit Risk Exposure of Bank Accounts of Commercial Banks, including project financing, object financing, commodity financing and income-producing real estate.

Article 5 Commercial banks may adopt the internal rating method or the regulatory mapping method to measure the credit risk and regulatory capital requirements of specialized loans.

Article 6 In case a commercial bank adopts the internal rating method, the internal rating system of specialized loans shall meet the requirements of the Guidelines on Supervising the Internal Rating System of the Credit Risks of Commercial Banks, and when estimating the default risk exposure, it shall fully consider the impact of continuing the grant of loans for promoting the assets formed by the loans put into operation after the debtor breaks the agreement so as to ensure the prudence of risk estimation.

Article 7 In case a commercial bank adopts the internal rating method, it shall measure the regulatory capital requirements of specialized loans according to the Rules for Calculating the

Capital Adequacy Ratio of Commercial Banks.

Article 8 In case the internal rating system of specialized loans of a commercial bank fails to meet the requirements of the Guidelines on the Supervising the Internal Rating System of the Credit Risks of Commercial Banks, the regulatory mapping method shall be adopted to measure the capital requirements of specialized loans.

Article 9 A commercial bank may adopt the regulatory mapping method to one or several subclasses of the specialized loans, and adopt the internal rating method to the other subclasses, but it shall not adopt different methods to the risk exposures of the same subclass at the same time.

Article 10 In case a commercial bank adopts the regulatory mapping method, the internal rating system of the specialized loans shall meet the following requirements:

1. The commercial bank shall adopt the one-dimensional rating to the specialized loans, and shall consider simultaneously in the rating the characteristics of both the debtors and the debts and the correlations between them so as to directly reflect the predicted losses.

2. The commercial bank shall establish at least 4 non-default levels and one default level.

Article 11 In case a commercial bank adopts the regulatory mapping method, the following facts shall be considered in the specialized loan rating:

1. For the projects financing rating, five factors, i.e., financial standing, political and legal environment, characteristics of the transactions in question, the strength of the project sponsors or debtors, and the security arrangements shall be taken into consideration. For the regulatory rating standards for project financing, see Annex 1 for details.

2. For the object financing rating, seven factors, i.e., financial standing, political and legal environment, transaction characteristics, operational risks, characteristics of the assets in questions, the strength of the project sponsors, and the security arrangements shall be taken into consideration. For the regulatory rating standards for object financing, see Annex 2 for

details.

3. For the commodities financing rating, five factors, i.e., financial standing, political and legal environment, characteristics of the assets in question, the strength of the project sponsors, and the security arrangements shall be taken into consideration. For the regulatory rating standards for commodity financing, see Annex 3 for details.

4. For the income-producing real estate rating, four factors shall be taken into consideration, i.e., financial standing, characteristics of the assets in questions, the strength of the project sponsors or developers, and the security arrangements. For the regulatory rating standards for income-producing real estate, see Annex 4 for details.

Article 12 In case a commercial bank adopts the regulatory mapping method, it shall map the internal rating results of specialized loans to the five regulatory ratings: “Excellent” “Good” “Fair” “Poor” or “Default”. The commercial bank shall ensure the consistency and stability of the mapping between the internal rating and the regulatory rating in light of the mapping between the internal rating and external rating and the mapping between the regulatory rating and the external rating.

1. The regulatory rating of “Excellent” shall correspond to the external rating of BBB- or above.

2. The regulatory rating of “Good” shall correspond to the external rating of BB+ or BB.

3. The regulatory rating of “Fair” shall correspond to the external rating of BB- or B+.

4. The regulatory rating of “Poor” shall correspond to the external rating of B or C-.

5. The regulatory rating of “Default” shall not be applicable for mapping with the external rating.

Article 13 Definition of the ratings: Excellent, Good, Fair, Poor and Default as mentioned in the preceding paragraph:

1. The regulatory rating of “Excellent” refers to that the bank has sufficient and stable cash flow to be produced in the future from the assets formed by the loans, has a very strong market competitive capacity and very strong sponsors, has made all the security arrangements, and is able to repay the debts even if the economy and industry face continuous and serious problems.

2. The regulatory rating of “Good” refers to that the bank has sufficient and stable cash flow to be produced in the future from the assets formed by the loans, has a good market competitive capacity and strong sponsors, has made all the security arrangements, but may be unable to fully repay the debts if the economy and industry face continuous and serious problems.

3. The regulatory rating of “Fair” refers to that the bank has sufficient cash flow to be produced in the future from the assets formed by the loans, has a fair market competitive force and sponsors with fair strength, and there are defects in the security arrangements so that the cash flow is not stable enough, and the bank is very weak in defending against economic recessions and industrial fluctuations.

4. The regulatory rating of “Poor” refers to that there is great uncertainty in the cash flow to be produced in the future from the assets formed by the loans, the bank is very weak in market competitiveness and the strength of the sponsors is very poor so that the bank’s solvency largely depends on the improvement of the economic environment and market demands, otherwise it may break the contracts.

5. The regulatory rating of “default” refers to that the bank already broken the contracts according to the definition of default in the Guidelines on the Supervising the Internal Rating System of the Credit Risks of Commercial Banks.

Article 14 Where a commercial bank adopts the regulatory mapping method, if the internal rating standards of the specialized loan are not consistent with the regulatory rating standards, the commercial bank shall record the difference between the two, and explain the reasons and rationality for the existence of the difference to the regulatory department, prove the mapping between the internal rating and the regulatory rating, and ensure the consistency in the main characteristics of both. The commercial bank shall ensure that overthrow of its internal rating will not lead to the invalidity of the mapping course.

Article 15 The five regulatory ratings of specialized loans shall respectively correspond to the specific risk weights, which are specifically as follows:

1. If the regulatory rating is “Excellent”, the risk weight shall be 70%.

2. If the regulatory rating is “Good”, the risk weight shall be 90%.

3. If the regulatory rating is “Fair”, the risk weight shall be 115%.

4. If the regulatory rating is “Poor”, the risk weight shall be 250%.

5. If the regulatory rating is “default”, the risk weight shall be 0%.

Article 16 If a commercial bank or a regulatory department considers that there will be great fluctuations in the rental income, sales revenue or revenue from the transfer of the real estate to which income-producing real estate loans are made, it may uplift the risk weight thereof:

1. If the regulatory rating is “Excellent”, the risk weight shall be 95%.

2. If the regulatory rating is “Good”, the risk weight shall be 120%.

3. If the regulatory rating is “Fair”, the risk weight shall be 140%.

Article 17 With regard to the specialized loans that meet any of the following conditions, if the regulatory rating is “Excellent”, the risk weight shall be 50%; if the regulatory rating is “Good”, the risk weight shall be 70%:

1. The remaining term of the loan is less than two and half years.

2. The regulatory department believes that the standards on credit and rating of the commercial bank are more prudent than its regulatory rating standards.

Article 18 The five regulatory ratings of the specialized loans shall correspond to the specific predicted loss ratios, to be specific:

1. If the regulatory rating is “Excellent”, the expected loss ratio shall be 0.4%.

2. If the regulatory rating is “Good”, the expected loss ratio shall be 0.8%.

3. If the regulatory rating is “Fair”, the expected loss ratio shall be 2.8%.

4. If the regulatory rating is “Poor”, the expected loss ratio shall be 8%.

5. If the regulatory rating is “default”, the expected loss ratio shall be 50%.

Article 19 With regard to the specialized loans that meet any of the following conditions, if the regulatory rating is “Excellent”, the expected loss ratio shall be 0%, and if the regulatory rating is “Good”, the expected loss ratio shall be 0.4%:

1. The remaining term of loan is less than two and half years.

2. The regulatory department believes that the standards on the credit and rating of the commercial banks are more prudent than its regulatory rating standards.

Article 20 The Annex 1, 2, 3 and 4 are a component part of these Guidelines.

Article 21 These Guidelines adopt the Standard & Poor’ s rating symbols, but do not provide for the selection of external credit rating companies by commercial banks, and the commercial banks may choose the rating results of the rating companies at their discretion so as to keep their continuity.

Article 22 The power to interpret these Guidelines shall remain with the China Banking Regulatory Commission.

Article 23 These Guidelines shall come into force on October 1, 2008; and the calculating rules for the regulatory capital requirements shall come into force on the date when the approval for implementing the new capital accord is obtained from the CBRC.

Annex 1: Regulatory Rating Standards for Project Financing

Annex 2: Regulatory Rating Standards for Object Financing

Annex 3: Regulatory Rating Standards for Commodity Financing

Annex 4: Regulatory Rating Standards for Income-producing Real Estate