

# The banking market competition and lending decision behavior in China

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## **Abstract:**

Bank competitions are more complicated since the structure involves two competitions, one in deposit market and the other in loan market. Most governments have significant intervention and some of them regulate the banking industry heavily. This unique industry feature makes the banking market characteristics different in many different countries, and the banks behavior and decision making highly depends on the local market conditions. The banks play important role in policy transmission and affect the economy development, which makes it crucial to understand the banking market structures and influence. This study explores the banking market structure, influence of market power on the banking behavior in a highly regulated environment, the Chinese market. By using the collected financial report information, the research analyzes the market structure and power on profitability and lending decisions. The results show that similar to most of bank markets, the lending market concentration has positive contribution to profit by increasing the loan rate, but the deposit market experience lower deposit rates in more concentrated market. The market power shows the differentiated competition feature compare with bank market in many other countries. The banks compete in loan quality by offering a lower loan rate, relying on higher leverage and lower the bad debt to generate higher profit, rather than offer higher loan rate to maximize the profit when they have higher market power. Furthermore, the smaller banks are not capable to compete in such a way since the larger size is required to cover the monitoring and operating cost, such strategy is infeasible when the scale is too small, and banks need to charge high enough loan rate to generate enough profit to cover operating costs.

**Keywords:** Bank competition, banking regulation, market structure, market power, efficiency, bad debt, profitability