

# Zhuhai Rural Commercial Bank Co., Ltd.

## Initial Issuer Report

### Summary

Issuer Rating	BBB-
Outlook	Stable
Location	China
Industry	Banking
Date	3 July 2023

### Major Operating Data of ZRCB

(RMB billion)	2021	2022
Total Asset	68.0	79.4
Revenue	1.57	1.55
Net Profit	0.54	0.59
ROA (%)	0.82	0.79
ROE (%)	9.59	7.51
Net Interest Margin(%)	2.11	1.96
Non-Performing Loan Ratio (%)	1.25	1.38
Allowance Coverage Ratio (%)	218.3	196.6
Capital Adequacy Ratio (%)	15.89	20.59
Core Tier 1 Capital Adequacy Ratio (%)	11.89	17.19

Source: ZRCB and Lianhe Global's calculations

**Lianhe Ratings Global Limited (“Lianhe Global”) has assigned ‘BBB-’ global scale Long-term Issuer Credit Rating with Stable Outlook to Zhuhai Rural Commercial Bank Co., Ltd.**

### Summary

The Issuer Rating reflects Zhuhai Rural Commercial Bank Co., Ltd. (“ZRCB”)’s established strong network in Zhuhai, strong capitalization after the private placement and adequate liquidity. In addition, we expect that there is a high possibility that the Zhuhai government would provide strong support to ZRCB if needed, considering their strong linkage. The rating also considers ZRCB’s limited operating scale, high concentration risks and narrowing net interest margin.

The Stable Outlook reflects our expectation that ZRCB will maintain its market position in Zhuhai and its linkage with the Zhuhai government while maintaining the capital adequacy ratio and liquidity ratio at the level which is commensurate with its credit profile

### Rating Rationale

**Established Strong Network in Zhuhai:** ZRCB, formerly known as Zhuhai Rural Credit Union, is a local bank in Zhuhai with a long operating history and the largest number of business sites covering whole Zhuhai, including its rural areas and three islands. It was ranked 8th in total deposit scale and top 3 in personal deposit scale consistently among banks operating in Zhuhai. The total deposit scale was behind stated-owned giants but ahead of an array of national players. The strong network provides stable funding to ZRCB. Customer deposits contributed over 80% to the bank’s total liabilities, of which c. 70% were personal deposits.

**Strong Capitalization and Adequate Liquidity:** ZRCB completed a sizeable private placement of RMB3.7 billion in 2022, lifting its capital adequacy ratio significantly to 22.44% at completion, a well above average level, from 13.95% at end-June 2022. This could greatly enhance the bank’s loss absorption capacity and viability and support its business growth. Yet we believe this high capital adequacy ratio was an exceptional case (let alone any further large-scale capital injection). We expect it to decrease gradually as the bank expands its assets in the next two to three years while staying at a healthy level.

ZRCB’s liquidity was adequate, given that the bank maintained a sizeable amount of highly liquid assets such as government and financial bonds. Its liquidity matching ratio also stayed at a relatively high level.

**Linkage with the Zhuhai government:** The Zhuhai government holds 43.22% shares of ZRCB through six SOEs in Zhuhai, and the Guangdong Rural Credit Union has turned over the management control of ZRCB to the Zhuhai government since 2021. Moreover, ZRCB is a major financial institution in Zhuhai, which is important in promoting local economic growth, especially in supporting micro, small and medium enterprises (“MSMEs”) and rural development and maintaining regional financial stability. Therefore, we expect that there is a high possibility that the Zhuhai government would provide strong support to ZRCB if needed.

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### Applicable Criteria

[Banking Rating Criteria](#)  
 (20 March 2023)

**Limited Operating Scale; High Concentration Risks:** ZRCB's operating scale is small given its nature as a rural commercial bank, putting it at a disadvantaged position in respect to its pricing power, product sophistication and economies of scale.

ZRCB adopts a credit policy supporting agriculture and MSMEs, which is in accordance with the regulatory requirements and the bank's own endowment. However, these borrowers are usually riskier than large corporates as they typically lack financial, management and other necessary resources to withstand adverse economic conditions. The asset quality of ZRCB's loans was under pressure as the economy was weak amid the covid pandemic and property market downturn, which has impaired borrowers, especially MSMEs' loan repayment ability.

ZRCB diversifies its loan portfolio by limiting large exposures to a single borrower. However, the sector concentration of its loans was moderately high. At end-2022, retail and wholesale sector contributed a moderately high proportion in ZRCB's loan portfolio, and this sector had a relatively high non-performing loan ratio. Also, ZRCB can only operate its lending business in Zhuhai due to regulatory requirement. Zhuhai is an important city in Guangdong-Hong Kong-Macao Greater Bay Area, yet the bank is more susceptible to changes in regional economic conditions in Zhuhai.

**Narrowing Net Interest Margin:** ZRCB's operating revenue was mainly driven by interest income arising from loans and bond investments. The fee and commission incomes were increasing but only contributed a small fraction of the bank's total revenue. ZRCB's net interest margin, however, demonstrated a downward trend between 2020 and 2022, which undermined the bank's profitability. This was mainly because the lending rate was lowered by the charge and rate cut policy to support the real economy. In addition, ZRCB faces intensive competition among banks in Zhuhai, and its funding costs are higher than its larger competitors.

## Rating Sensitivities

We would consider downgrading ZRCB's rating if there is 1) a significant decrease in its capital adequacy, or 2) a notable deterioration in its asset quality, or 3) a weakened funding structure, or 4) a perceived weakening linkage between the Zhuhai government and ZRCB.

We would consider upgrading ZRCB's rating if it were to 1) improve its operating scale without significantly compromising its capital adequacy and asset quality, and 2) lower the concentration of its loans portfolio, and 3) improve its profitability.

## Company Profile

ZRCB, formerly known as Zhuhai Rural Credit Cooperative, was founded in 1952. ZRCB is a locally incorporated bank and is the largest bank in Zhuhai in terms of agricultural loans and the number of micro, small and medium enterprises ("MSMEs") customers in Zhuhai.

Restructured into a joint-stock commercial bank in December 2012, ZRCB was formerly managed by the Guangdong Rural Credit Union ("GDRC") before transferring the management right to the Zhuhai government in August 2021.

In 2022, ZRCB issued 1,321 million shares through a private placement, raising RMB3.70 billion and increasing its capital stock to RMB3.97 billion. The private placement was aimed at supporting the business development of ZRCB. The shareholders who participated in the private placement were mainly state-owned enterprises ("SOEs") in Zhuhai. After the private placement, 43.2% of ZRCB's shares were held by SOEs in Zhuhai and 6.6% were held by a SOE of Guangdong Province.

Considering that ZRCB is a financial institution under Zhuhai government's administration, and the Zhuhai government holds a significant stake in ZRCB through SOEs in Zhuhai, we expect that the Zhuhai government will likely provide support to ZRCB if needed.

## Business Profile

ZRCB's main business lines include corporate banking, personal banking and financial market businesses. The bank actively provides inclusive financial services in Zhuhai. In 2020, 2021 and 2022, ZRCB's total operating revenue was RMB1,602 million, RMB1,574 million and RMB1,545 million, respectively.

Deposit Structure (RMB million)	2020		2021		2022	
	Amount	%	Amount	%	Amount	%
Corporate customers:	17,852	35.5	17,037	32.1	16,718	29.2
Individual customers:	31,650	62.9	35,085	66.1	39,340	68.8
Interest accrued	842	1.7	988	1.9	1,137	2.0
<b>Total</b>	<b>50,344</b>	<b>100.0</b>	<b>53,110</b>	<b>100.0</b>	<b>57,195</b>	<b>100.0</b>

Source: ZRCB

Loan Structure (RMB million)	2020		2021		2022	
	Amount	%	Amount	%	Amount	%
Corporate loans and advances:	20,264	60.7	21,604	57.4	24,674	58.5
Personal loans	13,074	39.2	16,012	42.5	17,456	41.4
<b>Total</b>	<b>33,393</b>	<b>100.0</b>	<b>37,672</b>	<b>100.0</b>	<b>42,192</b>	<b>100.0</b>

Source: ZRCB

## Corporate banking business

ZRCB's corporate banking segment focuses on supporting agriculture and MSMEs. As the bank actively underwrote corporate loans to the real economy, such as MSMEs in the agriculture, wholesale and retail sectors, its corporate loan balance grew steadily between 2020 and 2022. However, the corporate deposit was under pressure over the same period due to the weak deposit supply from MSMEs amid the economic downturn.

## Personal banking business

ZRCB has been promoting the development of retail banking in recent years. Its retail transformation began to bear fruit, with both personal deposit and loan businesses maintaining rapid growth between 2020 and 2022. ZRCB has developed a strong network covering urban and rural areas in Zhuhai, bringing growing personal savings deposits to the bank. In 2020, 2021 and 2022, personal savings deposits of ZRCB were RMB31.7 billion, RMB35.1 billion and RMB39.3 billion, respectively.

For retail loans, ZRCB mainly focused on personal business and mortgage loans, usually secured by collaterals such as borrowers' properties. The outstanding personal consumption loans, typically unsecured, were relatively small. Between 2020 and 2022, retail loans of ZRCB were RMB13.1 billion, RMB16.0 billion and RMB17.5 billion, respectively.

ZRCB was also developing its wealth management services. However, given the bank's relatively small high net worth client base and limited product lineup, its assets under management were small at end-2022, compared to larger competitors.

## Financial Market Business

ZRCB's investment assets grew significantly between 2020 and 2022, dominated by bond investment (including certificates of deposit). ZRCB's bond investment strategy is prudent and focuses on liquidity management. At end-2022, invested bonds mainly included treasury bonds, government bonds, financial institutions bonds, as well as highly rated corporate bonds, primarily issued by LIDCs in developed regions such as Jiangsu Province, Guangdong Province and Beijing. The bank also maintained its investment in non-traditional financing assets, such as asset management and trust beneficiary plans, at a relatively low level.

Investment Assets (RMB million)	2020		2021		2022	
	Amount	%	Amount	%	Amount	%
	Bond Investments	20,158	88.8	20,637	89.2	25,020
Asset management and trust beneficiary plans	313	1.4	823	3.6	2,046	6.6
Fund Investments	508	2.2	0	0.0	16.62	5.4
Others	1,436	6.3	1,375	5.9	3,581	6.2
Interest accrued	296	1.3	307	1.3	312	1.0
<b>Total investment</b>	<b>22,711</b>	<b>100.0</b>	<b>23,138</b>	<b>100.0</b>	<b>30,976</b>	<b>100.0</b>
Less: provision for impairment losses	-		-10		-42	
Net Investment	22,711		23,128		30,934	

Source: ZRCB

## Risk Profile

### Credit Policy and Profile

ZRCB adopts a credit policy following its strategic planning. For corporate loans, the bank has developed credit guidelines to support agriculture and MSMEs, prioritizing the allocation of credit resources to leading agriculture and manufacturing enterprises while limiting the growth of loans made to the property, construction, retail and wholesale sectors. The bank mainly targets clients with good credit records and stable incomes for personal loans.

Despite supporting agriculture and MSMEs in accordance with regulatory requirements, these borrowers are usually riskier than large corporates as they typically lack financial, management and other necessary resources to withstand adverse economic conditions. In addition, the bank faces difficulties in assessing their creditworthiness due to information asymmetry as MSMEs usually have minimal public information, visible operating history, and less reliable financial information.

Regarding risk control measures, the banks usually required collateral, mainly residential and commercial properties and production plants. The bank also strictly limits the concentration of loans to certain industries and borrowers. However, given its nature as a rural commercial bank, ZRCB's operation is inevitably concentrated in Zhuhai and therefore is more susceptible to changes in regional economic conditions.

ZRCB's credit concentration in terms of borrowers decreased between 2020 and 2022. In contrast, the industry concentration increased, with retail and wholesale remaining as the largest borrowing sector of the bank and contributing 63.83% to the bank's NPLs at end-2022.

**Credit Concentration Profile by Borrower**

	2020	2021	2022
Gross loan to the single largest borrower/net capital (%)	5.1	5.7	3.7
Gross loan to top 10 customers/net capital (%)	37.5	38.7	28.6

Source: ZRCB

**Credit Concentration Profile by Industry**

2020		2021		2022	
Industry	(%)	Industry	(%)	Industry	(%)
Wholesale and retail	27.9	Wholesale and retail	31.9	Wholesale and retail	33.6
Manufacturing	13.9	Manufacturing	14.0	Manufacturing	15.2
Real estate	9.5	Real estate	7.0	Construction	8.0
Construction	8.0	Construction	6.8	Real estate	7.4
Lease and business services	3.5	Lease and business services	2.7	Accommodation and catering	3.0
<b>Total</b>	<b>62.6</b>	<b>Total</b>	<b>62.3</b>	<b>Total</b>	<b>67.2</b>

Source: ZRCB

**Market Risk**

ZRCB's market risk was manageable. The bank's financial investments mainly included government bonds, financial bonds and highly rated corporate bonds, most of which were held-to-maturity assets. The bank has low proprietary trading positions and has little involvement in foreign exchange activities. However, ZRCB has few tools to hedge interest rate risks since it has no derivatives trading qualification yet.

**Operational Risk**

ZRCB's operational risk was manageable. The bank continues to improve the internal control system, strengthen the inspection and supervision, and increase the punishment for violations and disciplinary actions, striving to build a long-term mechanism of prevention, control and management of cases with five elements: education, control, supervision, responsibility and punishment. In recent years, the bank has further established and improved various management systems and business operation procedures and carefully reviewed and supplemented the original internal control structure and systems, focusing on corporate business, retail business, operation management, financial accounting and technology information risk management, further made solid efforts in case prevention, internal control and production safety, and the whole bank has operated safely and steadily throughout years without any material accident.

**Financial Profile**
**Capital Adequacy**

ZRCB's capital adequacy ratio exceeded the regulatory requirements between 2020 and 2022. Especially it increased to 20.59% at end-2022 from 15.89% at end-2021, as the bank completed a private placement of RMB3.7 billion, enlarging its net capital to RMB10.7 billion (end-2021:RMB6.6 billion). This significantly enhanced its loss absorption capacity and viability. However, we believe it was an exceptional case (let alone any further large-scale capital injection), and we expect ZRCB's capital adequacy ratio to decrease gradually in the next two to three years as the bank expands its assets after the private placement while staying at a healthy level.

**ZRCB's Capital Adequacy**

(RMB million)	2020	2021	2022
Total Risk-weighted assets	38,481	41,951	51,766
<b>Capital adequacy ratio (%)</b>	<b>16.59</b>	<b>15.89</b>	<b>20.59</b>
<b>Core tier 1 capital adequacy ratio (%)</b>	<b>12.33</b>	<b>11.89</b>	<b>17.19</b>

Source: ZRCB and Lianhe Global's calculations

**Asset Quality**
**ZRCB's Asset Structure:**

(RMB million)	2020		2021		2022	
	Amount	%	Amount	%	Amount	%
Cash and deposits with the central bank	5,039	7.9	4,774	7.0	4,407	5.6
Deposits and placements with banks and other financial institutions	2,789	4.4	1,812	2.7	1,971	2.5
<b>Loans and advances to customers</b>	<b>32,436</b>	<b>50.9</b>	<b>36,651</b>	<b>53.9</b>	<b>41,056</b>	<b>51.7</b>
<b>Investment Assets</b>	<b>22,711</b>	<b>35.6</b>	<b>23,128</b>	<b>34.0</b>	<b>30,934</b>	<b>38.9</b>
Others	750	1.2	1,651	2.4	1,078	1.4
<b>Total Assets</b>	<b>63,725</b>	<b>100.0</b>	<b>68,017</b>	<b>100.0</b>	<b>79,632</b>	<b>100.0</b>

Source: ZRCB and Lianhe Global's calculations

ZRCB's asset size grew steadily between 2020 and 2022, with a moderate growth rate of 5.9% and 6.7%, respectively. It then grew significantly by 17.1% at end-2022, owing to private placement during the year.

The bank's assets mainly consisted of loans and financial investments, representing 51.7% and 38.9% of its total assets at end-2022, respectively. The former one mainly loaned to MSMEs in retail and wholesale, manufacturing, construction and property sectors. That also included mortgages and personal loans for business and consumption purposes. The latter primarily comprised investments in government, financial institutions, and highly rated corporate bonds.

ZRCB's off-balance sheet activities mainly included issuing bank acceptances, letters of credit and letters of guarantee, amounting to RMB1,156 million at end-2022.

**ZRCB's Loans Quality**

(RMB million)	2020		2021		2022	
	Amount	%	Amount	%	Amount	%
Normal loans	30,387	91.2	34,602	92.0	39,098	92.8
Special mention loans	2,527	7.6	2,538	6.8	2,451	5.8
Non-performing loans	424	1.27	471	1.25	581	1.38
<b>Total</b>	<b>33,338</b>	<b>100</b>	<b>37,616</b>	<b>100</b>	<b>42,130</b>	<b>100</b>
Allowance coverage ratio (%)	-	225.7	-	218.3	-	196.6

Source: ZRCB and Lianhe Global's calculations

The asset quality of ZRCB's financial investments was largely stable in 2022, while that of loans was under pressure as the weak economy amid the covid pandemic and property market downturn has impaired borrowers, especially MSMEs' loan repayment ability. As a result, ZRCB's NPLs and overdue loans' share increased, reaching 1.38% and 2.93% at end-2022, respectively (end-2021:1.25% and 2.35%). The bank's allowance coverage ratio was also decreasing but stayed at a sufficient level of 196.6% at end-2022. Considering the under-pressure loan quality, we expect ZRCB's allowance coverage to decrease in the next two to three years.

## Profitability

ZRCB's operating revenue was mainly driven by interest income arising from loans and bond investments and supplemented by investment income, which was rather volatile between 2020 and 2022. The fee and commission income were increasing over the same period yet only contributed a small fraction to ZRCB's total revenue.

ZRCB's operating revenue demonstrated a downward trend between 2020 and 2022, primarily due to the narrowing net interest margin, as the authority lowered the lending rate to support the economy. In addition, ZRCB faces intensive competition among banks in Zhuhai. Its funding costs were higher compared with larger competitors. In contrast, the bank's operating expenses showed an upward trend in the past three years.

ZRCB's ROE dropped significantly to 7.51% in 2022 from 9.59% in 2021, partially owing to its private placement in 2022. We expect it to recover gradually in the next two to three years as the incremental capital would support the bank's business growth.

### ZRCB's Revenue Structure

(RMB million)	2020	2021	2022
<b>Operating revenue:</b>	<b>1,602</b>	<b>1,574</b>	<b>1,545</b>
- Net interest income	1,416	1,298	1,303
- Net fee and commission income	30	33	40
- Investment income	153	211	134
<b>Operating expenses:</b>	<b>(1,000)</b>	<b>(978)</b>	<b>(880)</b>
- Impairment loss of assets	(398)	(322)	(192)
<b>Net profit</b>	<b>510</b>	<b>541</b>	<b>585</b>
Net interest margin (%)	2.38	2.11	1.96
Net profit/average total assets (%)	0.82	0.82	0.79
Return on average equity (%)	9.54	9.59	7.51

Source: ZRCB and Lianhe Global's calculations

## Funding and Liquidity

### ZRCB's Liabilities Structure

(RMB million)	2020		2021		2022	
	Amount	%	Amount	%	Amount	%
Market funding	5,714	9.8	5,564	8.9	8,853	12.7
Customers deposits	50,344	86.5	53,110	85.3	57,195	82.1
- Personal deposits	31,650	54.4	35,085	56.4	39,340	56.5
Others	2,161	3.7	3,569	5.7	3,585	5.2
<b>Total liabilities</b>	<b>58,219</b>	<b>100.0</b>	<b>62,244</b>	<b>100.0</b>	<b>69,634</b>	<b>100.0</b>

Source: ZRCB and Lianhe Global's calculations

ZRCB's liabilities structure was largely stable between 2020 and 2022, with customer deposits contributing over 80% to the total liabilities. The personal deposits grew steadily to RMB39.3 billion at end-2022 from RMB31.7 billion at end-2020, representing a compound annual growth rate of 11.49%, providing relatively stable funds to the bank. This benefited from ZRCB's strong and established network in Zhuhai. However, the fixed deposits proportion was high (58.9%) at end-2022, resulting in a higher fund cost.

In 2022, ZRCB actively raised market funds from policy banks to support the real economy, pushing the market funding balance to RMB8,853 million at end-2022 from RMB5,564 million at

end-2021. The bank also expanded its funding sources by cooperating with Macao's financial institutions.

#### ZRCB's Liquidity Indicator

	2020	2021	2022
Liquidity Ratio (%)	85.96	83.29	72.23
Gross loans and advances to customer deposits (%)	62.13	66.46	70.68
Liquidity coverage ratio (%)	245.94	222.72	137.31

Source: ZRCB and Lianhe Global's calculations

ZRCB's liquidity was adequate, given that the bank maintained a sizeable amount of highly liquid assets such as government and financial institutions bonds. Its liquidity coverage ratio, however, dropped significantly to 137.3% at end-2022 from 222.7% at end-2021 due to the increase in the proportion of short-term deposits and the increasing use of repurchases to obtain funds during the year.

According to the management, ZRCB was able to survive for more than 90 days under liquidity stress tests. The bank also has contingent liquidity, including borrowing from the central bank through the standing lending facility, emergency use of required reserves, borrowing from GDRC, as well as support from its state-owned shareholders.

### External Support

ZRCB is a financial institution under the Zhuhai government's administration. The Zhuhai government holds 43.2% shares of ZRCB through six SOEs in Zhuhai. The bank is important in promoting local economic growth, especially in supporting MSMEs and rural development and maintaining regional financial stability. Therefore, we expect that there is a high possibility that the Zhuhai government would provide strong support to ZRCB if needed, considering their strong linkage.

### Appendix: ZRCB's Top 10 Shareholders

股东名称	股东持股数量	单个股东持股	关联方合并持股
		比例 (%)	比例 (%)
珠海华发集团有限公司	262,242,953	6.61%	9.90%
珠海华发投资控股集团有限公司	130,714,285	3.29%	
珠海科创弘源投资管理有限公司	356,225,590	8.97%	8.97%
珠海大横琴发展有限公司	321,428,571	8.10%	8.10%
横琴金融投资集团有限公司	321,428,571	8.10%	8.10%
珠海格力建设投资有限责任公司	278,571,428	7.02%	8.10%
珠海市市场经营集团有限公司	42,857,142	1.08%	
广东能源集团财务有限公司	262,242,953	6.61%	6.61%
温氏食品集团股份有限公司	262,242,953	6.61%	6.61%
河北普阳实业集团有限公司	158,935,122	4.00%	4.00%
珠海鸣志房地产有限公司	118,522,472	2.99%	2.99%
成都地方建筑机械化工程有限公司	63,548,688	1.60%	1.60%



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