

Xiamen International Bank Co., Ltd.

Initial Issuer Report

Summary

Issuer Rating	A-
Outlook	Stable
Location	China
Industry	Banking
Date	4 September 2023

Lianhe Global has assigned 'A-' global scale Long-term Issuer Credit Rating with Stable Outlook to Xiamen International Bank Co., Ltd. ("XIB" or "the bank")

Summary

The Issuer Rating reflects Xiamen International Bank Co., Ltd. ("XIB")'s established network in economically advanced regions in mainland China, as well as Hong Kong and Macau, stable funding sources and adequate liquidity. In addition, we expect that there is a high possibility that the Fujian Provincial People's Government ("the Fujian government") would provide strong support to XIB if needed, considering their strong linkage. The rating also considers XIB's under-pressure capital adequacy, asset quality, and weakening profitability.

The Stable Outlook reflects our expectation that XIB will maintain its established market position and its linkage with the Fujian government while maintaining the capital adequacy ratio and liquidity ratio at the level commensurate with its credit profile.

Major Operating Data of XIB

(RMB billion)	2021	2022
Total Asset	1,007.2	1,088.1
Revenue	16.8	17.1
Net Profit	5.8	5.9
ROA	0.59%	0.56%
ROE	7.78%	7.11%
Net Interest Margin	1.66%	1.47%
Non-Performing Loan Ratio	1.06%	1.26%
Allowance Coverage Ratio	202.73%	168.42%
Capital Adequacy Ratio	11.73%	11.69%
Core Tier-1 Capital Adequacy Ratio	9.44%	9.03%

Rating Rationale

Local Franchise with International Expansion: XIB, headquartered in Fujian's Xiamen city, is one of the major city commercial banks in Fujian. The bank has an established network in economically advanced regions in China, such as Fujian Province, Guangdong Province, Yangtze River Delta Area, and Bohai Rim Region. XIB also has a subsidiary in Hong Kong (Chiyu Bank) and a subsidiary in Macau (Luso International Bank). The former has been deeply rooted in Hong Kong for over eighty years, while the latter is one of the major commercial banks in Macau. Two subsidiary banks enable XIB to provide comprehensive cross-border financial solutions, strengthening XIB's international positioning and synergy effect between onshore and offshore businesses.

Linkage with Local Government: XIB is one of three financial institutions under the Fujian government's administration, promoting local economic development and maintaining regional financial stability. The bank has a strong linkage with the government, including significant government ownership, senior management appointments and supervision of major strategic planning and decisions. At end-2022, among XIB's top ten shareholders, four were ultimately controlled by the Fujian government with an aggregate shareholding of 28.3%, while the Xiamen government ultimately controlled two with an aggregate shareholding of 7.8%.

In addition, XIB was the first Sino-foreign joint venture bank in China. Given XIB's unique background, the bank plays a special role in providing financial services to and uniting oversea Chinese individuals and corporates.

Stable Funding Sources and Adequate Liquidity: XIB's funding sources were largely stable. The customer's deposits maintained steady growth in the past three years, most of which were time deposits. The personal deposits increased significantly in 2022 due to the enlarged retail client base during the year. XIB's liquidity was adequate, given that the bank maintained a sizeable amount of highly liquid assets such as government and financial bonds. Its liquidity coverage ratio remained relatively high in the past three years despite

Source: XIB and Lianhe Global

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Applicable Criteria

Banking Rating Criteria
 (20 March 2023)

some fluctuation, which was 202.43% at end-2022, while the net stable fund ratio has been steady at between 105% and 110% over the same period. The bank's liquidity coverage ratio matching ratio also stayed at a relatively high level, which was 131.09% at end-2022.

The Development of Corporate Banking Segment: Corporate banking is XIB's most important business segment. However, its development was slowing down in the past three years. XIB's corporate loans balance growth rates were 6.8%, 1.2%, -0.2% in 2020, 2021, and 2022, respectively. This was because XIB was retreating corporate loans from provinces without branches under regulatory requirements, plus the Covid's impact on the economy suppressed credit demand in the past three years.

XIB refocus on developing local corporate customers in where the bank has branches such as Fujian, Guangdong, Shanghai and Beijing to fill the gap. In addition, XIB actively promotes loans to micro, small, and medium enterprises, following regulatory guidance, to expand its corporate customer base. We expect XIB's corporate banking segment to resume steady growth in the next two to three years as loans to corporate customers in provinces without branches have been largely exited.

Profitability: XIB's operating revenue fluctuated in the past three years, and its ROA and ROE were relatively low. The bank's operating revenue was mainly generated by net interest income and followed by investment income. Both XIB's net interest income and fee and commission income dropped in 2022, primarily due to the charge and rate cut policy to support the real economy and Covid's repetitive disruption in where XIB operates. XIB's net interest margin narrowed in 2022, following the trend of China's banking sector. XIB's funding costs were high as time deposits accounted for over 80% of the bank's total deposit. In addition, XIB's offshore subsidiaries faced rising deposit interest costs amid the US Federal Rate hikes.

Capital Adequacy and Asset Quality under Pressure: XIB's capital adequacy indicators decreased in 2022, yet they met regulatory requirements with some buffers. The decrease was mainly due to the significant increase in risk-weight assets as the bank enlarged its loan assets to support the real economy while the bank's capital replenishment plan, such as new issuance of equity, was still in progress. At the same time, challenging market conditions, such as narrowing net interest margins and increasing impairment loss amid the economic downturn, weakened the current endogenous growth of the bank's capital. We expect the total capital adequacy of XIB to improve upon the new issuance of capital bonds, while the core Tier-1 capital adequacy ratio to be under pressure as the bank's profitability remains weak.

XIB experienced deterioration in loan quality in 2022, with increases in special mention loans and non-performing loans as proportions of the total loan portfolio. This was mainly because the weak economy amid the Covid pandemic has impaired some borrowers' repayment ability. Nevertheless, XIB's NPL ratio (1.26%) was lower than the average level of city commercial banks (1.85%). However, given XIB's current low allowance coverage ratio, we expect the bank to face high assets impairment charge pressure, which could suppress its profitability in the next one to two years.

Rating Sensitivities

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

We would consider upgrading XIB's rating if it were to 1) improve its capital adequacy and asset quality significantly, and 2) improve its profitability, and 3) improve its business mix and loan portfolio diversification.

Company Profile

XIB, headquartered in Fujian's Xiamen city, was China's first Sino-foreign joint venture bank. The bank was established in 1985 with initial registered capital of HKD800 million.

In 2013, XIB was restructured as a Chinese-funded city commercial bank and subject to the administration of the Fujian government. After an array of capital increases and share expansions, XIB's registered capital was enlarged to RMB13.8 billion. Among XIB's top ten shareholders, four were ultimately controlled by the Fujian government with an aggregate shareholding of 28.32%, while the Xiamen government ultimately controlled two with an aggregate shareholding of 7.82%.

Business Profile

XIB's major business lines include corporate banking, retail banking and financial market. The bank is also developing its investment banking and asset management businesses. Boasting 12 provincial branches in mainland China, XIB primarily operates within economically advanced regions, such as Fujian Province, Guangdong Province, Yangtze River Delta Area, and Bohai Rim Region, accounting for 25.82 %, 22.44 %, 17.52 %, and 11.06 % of the bank's loans balance, respectively, at end-2022.

XIB also controls one subsidiary in Hong Kong (Chiyu Bank) and one in Macau (Luso International Bank), with ownership of 69.63% and 49.04%, respectively, at end-2022. Chiyu Bank, acquired by XIB in 2017, has been deeply rooted in Hong Kong for over 70 years, with a total asset of equivalent RMB162.4 billion at end-2022, while Luso International Bank is a major commercial bank in Macau with a total asset of equivalent RMB209.3 billion. Offshore subsidiaries enable XIB to provide comprehensive cross-border financial solutions, strengthening XIB's international positioning and synergy effect between onshore and offshore businesses. Moreover, XIB, Chiyu Bank and Luso International Bank are eligible for launching the Cross-boundary Wealth Management Connect Pilot Scheme, a key initiative of mutual market access between the capital markets of Mainland China, Hong Kong and Macao, allowing residents to invest in wealth management products distributed by banks in each other's market.

Deposit Structure

(RMB million)	2020		2021		2022	
	Amount	%	Amount	%	Amount	%
Corporate customers:	478,858	73.7	488,586	73.5	492,974	71.2
Individual customers:	162,836	25.1	160,854	24.2	186,596	28.0
Margin deposits and others	7,938	1.2	15,554	2.3	12,633	1.8
Total*	655,411	100.0%	671,495	100.0%	700,709	100.0%

Note: excluding interest accrued

Source: XIB

Loan Structure

(RMB million)	2020		2021		2022	
	Amount	%	Amount	%	Amount	%
Corporate loans and advances:	423,262	80.4	428,511	75.6	427,519	69.5

Personal loans	102,943	19.6	138,563	24.4	187,816	30.5
Total*	526,205	100.0	567,074	100.0	615,335	100.0

Note: excluding interest accrued
Source: XIB

Corporate banking business

Corporate banking is XIB's most important business segment. However, its development was slowing down in the past three years. The growth rates of XIB's corporate loans and advances' balance were 6.8%, 1.2%, -0.2% in 2020, 2021, and 2022, respectively. This was because XIB was retreating corporate loans from provinces without branches under regulatory requirements, plus the Covid's impact on the economy suppressed credit demand in the past three years.

XIB refocus on developing local corporate customers, mainly in Fujian and Guangdong, to fill the gap. In addition, XIB actively promotes loans to micro, small, and medium enterprises ("MSMEs"), following regulatory guidance, to expand its corporate customer base. The bank has formulated tailor-made credit products and policies for MSMEs and standardized the MSMEs' loan application and approval process to improve efficiency. We expect XIB's corporate banking segment to resume steady growth in the next two to three years as loans to corporate customers in provinces without branches have been largely exited.

Retail banking business

With the strategic transformation of retail banking, the segment is in a fast-development track, contributing 27.0% and 30.5% to the bank's deposit and loan balances at end-2022, respectively, up from 24.2% and 24.4% at end-2020. Xiamen International Bank expands its retail customer base by continuously cultivating local key customer groups, strengthening the ecological layout of diversified scenes and open banking development. The bank's total number of retail customers exceeded three million at end-2022, representing an increase of 0.9 million compared to the previous year. At the same time, XIB steadily improves customer value contribution by providing comprehensive services, such as personal loans and wealth management services. XIB's personal loans (including personal business loans) balance increased significantly to RMB187.8 billion at end-2022 from RMB102.9 billion at end-2020, representing a compound annual growth rate ("CAGR") of 35.1%.

Financial Market Business

XIB's total investment assets decreased by 5.1% to RMB282.5 billion at end-2021 from RMB296.8 billion at end-2020, as the bank gradually exited its relatively risky non-standard investments, such as asset management, trust beneficiary and debt financing plans. At end-2022, XIB's total investment assets increased by 8.4% to RMB306.0 billion, mainly consisting of bond investments (71.7%) and fund investments (17.1%). The bank's bonds portfolio mainly included government bonds, supplemented by financial institutions and corporate bonds, while the underlying assets of its fund investments were mostly bonds and money market funds. The non-standard investments' contribution dropped to 6.2% from 17.2% at end-2020 and 11.4% at end-2021.

The change in XIB's investment assets' structure is in accordance with the bank's strategy of prioritizing liquidity while maintaining the management and control of market and credit risks. XIB is also promoting the development of the financial market business by enhancing its research and trading capabilities.

Investment Assets (RMB million)	2020		2021		2022	
	Amount	%	Amount	%	Amount	%
Bond Investments	203,501	68.6	204,978	72.3	219,554	71.7
Fund Investments	26,873	9.1	29,771	10.5	52,253	17.1
Asset management, trust beneficiary and debt financing plans	51,145	17.2	32,258	11.4	18,922	6.2
Others	15,288	5.2	15,449	5.5	15,321	5.0
Total investment	296,907	100.0	282,456	100.0	306,050	100.0
Interest accrued	3,136		2,283		2,185	
Less: provision for impairment losses	(2,756)		(2,473)		(1,845)	
Net Investment	297,187		282,265		306,389	

Note: rounding differences exist
Source: XIB

Risk Profile

Credit Policy and Profile

With a focus on the developed coastal regions in China, including Fujian Province, Guangdong Province, Yangtze River Delta Area, and Bohai Rim Region, XIB provides credit policy support to local advantageous industries and key customers, while targets to strengthen support towards inclusive finance for MSMEs, green finance, and manufacturing industries.

XIB has set internal control requirements for concentration indicators and linked them to the bank's performance assessment. The bank has demonstrated relatively good control over the loan concentration. At end-2022, the bank's loan concentration to the largest group customer was 6.68%, and that to the largest single borrower was 3.10%, which accounted for 7.55% and 3.50% of the bank's tier-1 capital, respectively. Both figures were below the regulatory requirements of 15% and 20%, respectively. Moreover, XIB continues to support MSMEs, whose average loan balances were lower, to further diversify its loan portfolio. The top five industry concentration ratio decreased to 50.6% at end-2022 from 62.6% at end-2020.

From the perspective of risk mitigation measures, the bank primarily relied on collateral, mainly deposits, marketable securities, equity, real estate, land use rights, machinery and equipment. Collateralized loans accounted for 55.7% of XIB's total loan balance at end-2022.

The retail and wholesale sector stayed as the bank's largest borrowing sector, contributing 26.8% to the bank's total loan balance at end-2022, compared with 30.5% at end-2019. Yet this sector's non-performing loan ("NPL") ratio was relatively high and accounted for 24.8%, 60.9% and 35.4% of the XIB (excluding Chiyu Bank and Luso International Bank)'s new NPLs in 2020, 2021 and 2022, respectively, as the Covid pandemic severely hit the sector in the past three years.

Credit Concentration Profile by Borrower	2020	2021	2022
Gross loan to the single largest borrower/net capital (%)	2.8	2.7	3.1
Gross loan to top 10 customers/net capital (%)	21.5	20.5	17.2

Source: XIB

Credit Concentration Profile by Industry

2020		2021		2022	
Industry	%	Industry	%	Industry	%
Wholesale and retail	26.8	Wholesale and retail	22.0	Wholesale and retail	18.7
Water conservancy, environment and public facilities management	12.2	Real estate	10.2	Lease and business services	10.1
Real estate	10.1	Water conservancy, environment and public facilities management	9.9	Real estate	8.0
Lease and business services	7.6	Lease and business services	9.4	Water conservancy, environment and public facilities management	7.3
Financial industry	5.9	Financial industry	5.7	Financial industry	6.5
Total	62.6	Total	57.2	Total	50.6

Source: XIB

Market Risk

XIB's market risk was manageable. At end-2022, XIB maintained its market risk-weighted assets and market risk capital occupation at a moderate level. Its market risk indicators met regulatory requirements.

XIB mainly controls its market risk exposure for its financial investments by investing in government, financial institutions and highly rated corporate bonds with high liquidity and limiting their duration to below three years (end-2022: 2.84 years). At end-2022, over 85% of the bonds invested by XIB (excluding Chiyu Bank and Luso International Bank) were issued by local government and local investment and development companies ("LIDCs") in regions where XIB has branches, such as Beijing, Shanghai, Guangdong Province and Fujian Province. XIB also includes all the bond investments into the group's unified credit management system, and the approval standards for the bond investment limit of a specific issuer are the same as that of the credit facility limit.

Operational Risk

XIB has formulated operational risk management policies, and applied management tools such as operational risk and control self-assessment, key risk indicators, loss data collection. The bank continuously carries out the identification, assessment, monitoring and mitigation of operational risks, and timely formulates optimization plans or rectification measures for procedures with high residual risks, indicators that trigger warning signal and operational risk loss events. The bank advocates the concept of operational risk precaution and requires audit from the perspective of internal control, compliance and operational risk prevention and control before the issuance of rules and regulations and system design, to avoid operational risks caused by design defects or imperfections of the system, process and system. The bank has annual inspection plans for all business lines and institutions every year, covering all major businesses and key risk areas, and rectifies operational risks found in the inspection in a timely manner.

Financial Profile

Capital Adequacy

XIB's capital adequacy indicators decreased in 2022, yet they met regulatory requirements with some buffers. The decrease was mainly due to the significant increase in risk-weight assets as the bank enlarged its loan assets to support the real economy while the bank's capital replenishment plan, such as new issuance of equity, was still in progress. At the same time, challenging market conditions, such as narrowing net interest margins and increasing impairment loss amid the economic downturn, weakened the current endogenous growth of the bank's capital.

XIB plans to replenish its capital by issuing new shares and capital bonds, and it strives for the IPO of Xiamen International Investment Limited, its oversea investment platform holding the shares of Chiyu Bank and Luso International Bank. We expect the total capital adequacy of XIB to improve upon the issuance of RMB12 billion Tier 2 capital bonds, while the core Tier-1 capital adequacy ratio to be under pressure as the bank's profitability remains weak.

XIB's Capital Adequacy			
(RMB million)	2020	2021	2022
Total Risk-weighted assets	652,673	684,578	757,998
Capital adequacy ratio (%)	12.06	11.73	11.69
Core tier-1 capital adequacy ratio (%)	9.15	9.44	9.03

Source: XIB and Lianhe Global's calculations

Asset Quality

XIB's asset size remained steady growth between 2020 and 2022, with a CAGR of 7.0%. The asset structure of XIB was relatively stable in the past three years. The bank's assets mainly consisted of loans to customers and financial investments, representing 55.7% and 28.2% of its total assets at end-2022, respectively. The former was mainly loans to wholesale and retail, lease and business services, real estate, infrastructure and public facilities sector, as well as personal loans (including personal business loans). The latter primarily comprised investments in bonds (including government bonds, financial institutions and highly rated corporate bonds) and fund investments.

XIB's off-balance exposures mainly included financial derivatives, bank acceptances, letters of credit and letters of guarantee. At end-2022, the total size of off-balance exposures of XIB (excluding Chiyu Bank and Luso International Bank) was RMB646.4 billion.

XIB's Asset Structure:						
(RMB million)	2020		2021		2022	
	Amount	%	Amount	%	Amount	%
Cash and deposits with the central bank	57,481	6.0	64,405	6.4	57,306	5.3
Deposits and placements with banks and other financial institutions	61,611	6.5	80,097	8.0	90,443	8.3
Loans and advances to customers	516,621	54.4	557,249	55.3	605,787	55.7
Investment Assets	297,187	31.3	282,265	28.0	306,389	28.2
Others	17,246	1.8	23,153	2.3	28,190	2.6
Total Assets	950,146	100.0	1,007,169	100.0	1,088,115	100.0

*Note: rounding differences exist
Source: XIB and Lianhe Global's calculations*

XIB experienced deterioration in loan quality in 2022, with increases in special mention loans and non-performing loans as proportions of the total loan portfolio. This was mainly because the weak economy amid the Covid pandemic has impaired some borrowers' repayment ability. Nevertheless, XIB's NPL ratio was lower than the average level of city commercial banks (1.85%). At end-2022, XIB's allowance coverage ratio decreased to the lowest level of 168.42% in recent years.

XIB's Loans Quality

(RMB million)	2020		2021		2022	
	Amount	%	Amount	%	Amount	%
Normal loans	513,927	97.67	549,744	96.94	593,312	96.42
Special mention loans	7,884	1.50	11,344	2.00	14,274	2.32
Non-performing loans	4,394	0.84	5,986	1.06	7,749	1.26
Allowance coverage ratio (%)	-	259.80	-	201.73	-	168.42

Source: XIB and Lianhe Global's calculations

Profitability

XIB's operating revenue, primarily generated by net interest income and followed by investment income, fluctuated in the past three years. Both XIB's net interest income and fee and commission income dropped in 2022, primarily due to the charge and rate cut policy to support the real economy, and Covid's repetitive disruption in where XIB operates. XIB's funding costs were high as time deposits accounted for over 80% of the bank's total deposit. In addition, XIB's offshore subsidiaries faced rising deposit interest costs amid the US Federal Rate hikes. As a result, XIB's net interest margin narrowed to 1.47% in 2022 from 1.66% in 2021. XIB's ROA and ROE ratios demonstrated a downward trend in the past three years, following the trend of China's banking sector. Yet they were relatively low among its peers in 2022.

XIB's Revenue Structure

(RMB million)	2020	2021	2022
Operating revenue:	17,919	16,792	17,128
- Net interest income	13,754	13,879	12,731
- Net fee and commission income	2,000	1,442	1,409
- Investment income	3,116	2,706	2,948
- Gains and losses from changes in fair value	(553)	(266)	753
Operating expenses:	(11,695)	(11,043)	(11,250)
- Impairment loss of assets	(6,341)	(5,326)	(5,010)
Net profit	5,728	5,800	5,879
Net interest margin (%)	1.63	1.66	1.47
Net profit/average total assets (%)	0.61	0.59	0.56
Return on average equity (%)	8.69	7.78	7.11

Source: XIB and Lianhe Global's calculations

Funding and Liquidity

XIB's funding sources were largely stable. The customer's deposits maintained steady growth in the past three years, most of which were time deposits. The personal deposits increased significantly in 2022 due to the enlarged retail client base during the year. Yet the

sharp increase in borrowing from the central bank reduced the customer deposits as a percentage of total liabilities in 2022.

XIB's Liabilities Structure						
(RMB million)	2020		2021		2022	
	Amount	%	Amount	%	Amount	%
Market funding	207,518	23.6	228,350	24.6	248,786	24.8
Customers deposits	655,411	74.4	671,495	72.4	700,709	69.9
- Personal deposits	162,836	18.5	160,854	17.3	186,596	18.6
Others	17,443	2.0	28,056	3.0	52,460	5.2
Total liabilities	880,372	100.0	927,901	100.0	1,001,955	100.0

Source: XIB and Lianhe Global's calculations

XIB's liquidity was adequate, given that the bank maintained a sizeable amount of highly liquid assets such as government bonds. Its liquidity coverage ratio remained relatively high despite some fluctuation in the past three years, while the net stable fund ratio has been steady over the same period. The bank's liquidity coverage ratio matching ratio also stayed at a relatively high level.

XIB's Liquidity Indicator			
	2020	2021	2022
Liquidity Ratio (%)	104.97	125.25	110.59
Liquidity coverage ratio (%)	384.92	241.89	202.43
Net stable fund ratio (%)	109.14	106.94	107.08
Liquidity matching ratio (%)	116.93	136.45	131.09

Source: XIB and Lianhe Global's calculations

External Support

We expect that there is a high possibility that the Fujian government would provide strong support to XIB if needed. This considers XIB's strategic position as one of three financial institutions under the Fujian government's administration and a major city commercial bank in Fujian, promoting local economic development and maintaining regional financial stability, the strong linkage between the Fujian government and XIB, including the Fujian government's significant ownership of XIB, senior management appointments and supervision of major strategic planning and decisions. In addition, given XIB's unique background and strong overseas connections, the bank plays a special role in providing financial services to and uniting overseas Chinese individuals and corporates.

Appendix: XIB's Shareholder Structure at end-2022

	Shareholder	%
1	福建省福投资有限责任公司	12.05%
2	闽信集团有限公司	8.85%
3	中国工商银行股份有限公司	4.33%
4	福建投资企业集团公司	4.20%
5	厦门国贸控股集团有限公司	3.92%
6	厦门建发集团有限公司	3.90%
7	珠海铎创投资管理有限公司	3.39%
8	福建发展高速公路股份有限公司	3.22%
9	苏州苏高新科技产业发展有限公司	3.05%
10	华丽家族股份有限公司	2.92%

Source: XIB

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