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S&P Global
China Ratings

Credit Rating Report:

Shanghai Rural Commercial Bank Co., Ltd.

Issuer Credit Rating*: AAA_{spc}; Outlook: Stable

Rating Date: December 26, 2024
Date of Expiry: December 25, 2025

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Tear Sheet

Company Name	Rating Type	Current Rating	Rating Date	Outlook/CreditWatch
Shanghai Rural Commercial Bank Co., Ltd.	Issuer Credit Rating	AAA_{spc}	December 26, 2024	Stable

Rating Snapshot:

Industry Classification	Commercial Bank
Anchor	a+
— Business Position	0
— Capital and Earnings	0
— Risk Position	+1
— Funding and Liquidity	+1
— Holistic Adjustment	+1
Stand-alone Credit Profile	$aa_{spc}+$
Government Support	+1
Issuer Credit Rating	AAA_{spc}
Outlook/CreditWatch	Stable

Anchor: We apply an anchor of "a+" for commercial banks.

Business Position: SHRCB is one of the leading rural banks in China. It has an extensive network and solid customer base in Shanghai, especially in the municipality's suburbs. Its deposit and loan books have maintained steady growth.

Capital and Earnings: The bank has a strong capital base thanks to its adequate reserves. It maintains low credit cost through effective management in NIM and operating cost, which leads to healthy profitability.

Risk Position: Benefitting from the good credit environment in Shanghai and the bank's prudent risk management, the bank enjoys better asset quality metrics than the industry average. The bank's exposure to real estate and LGFVs is controllable.

Funding and Liquidity: Given its stable deposit base in Shanghai and prudent liquidity management, the bank is modestly reliant on wholesale funding. It maintains stable funding and adequate liquidity. Its financing costs in the interbank market are lower than regional banks' average.

Holistic Adjustment: It is one of the largest rural banks in China and has high capital adequacy. Its capital and earnings are resilient and not susceptible to risks from real estate and local governments' hidden debt. In general, we apply a one-notch upward holistic adjustment.

External Support: As a state-owned bank with close ties to the Shanghai government, SHRCB plays an important role in serving local small and micro enterprises (SMEs) and the agricultural sector. We consider the likelihood of the bank receiving government support in times of stress as high due to its high importance to the Shanghai government.

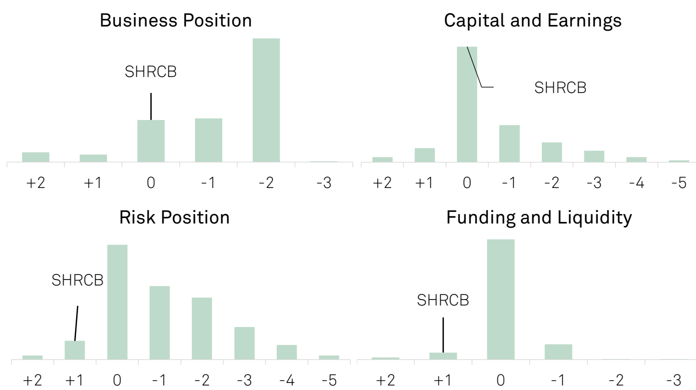
Company Overview: Incorporated in 2005, Shanghai Rural Commercial Bank Co., Ltd. ("SHRCB") has a solid business franchise in Shanghai. As of the end of June 2024, the bank reported total assets of 1.45 trillion RMB, net loans of 710.76 billion RMB, customer deposits of 1.07 trillion RMB. It generated a net income of 12.49 billion RMB in 2023, with an ROAE of 11.25%.

Key Metrics:

	2020	2021	2022	2023	2024.06
Total assets (bil.)	1,056.98	1,158.38	1,281.40	1,392.21	1,454.96
Customer deposits (bil.)	748.99	838.14	943.48	1,016.41	1,047.39
Net income (bil.)	8.42	10.05	11.39	12.49	7.14
Reported capital adequacy ratio (%)	14.40	15.28	15.46	15.74	17.15
Return on average equity (%)	10.89	11.30	11.22	11.25	N/A
Non-performing loan ratio (%)	0.99	0.95	0.94	0.97	0.97
Reserve coverage ratio (%)	419.17	442.50	445.32	404.98	372.42
Customer deposits/total debt (%)	76.70	78.99	80.25	79.67	78.60

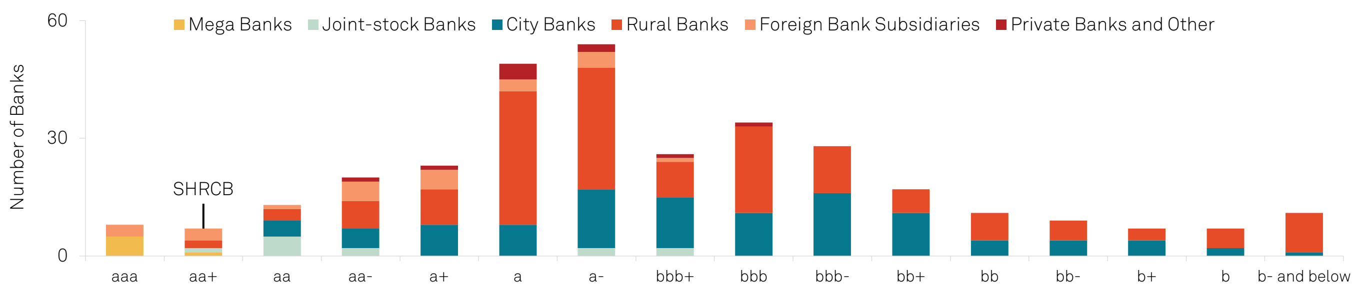
Source: SHRCB, collected and adjusted by S&P Global (China) Ratings.

Rating Factors of Stand-alone Credit Quality for Major Banks in China



Source: S&P Global (China) Ratings.

Distribution of Stand-alone Credit Quality of Major Banks in China



Note 1: Our assessment on issuer credit quality does not consider the likelihood of group or government support in times of stress but take into account the ongoing group or government support.

Note 2: The indicative issuer credit quality distributions expressed in this page are only our indicative views of credit quality derived from a desktop analysis based on public information without interactive review with any particular entity (except for solicited rating projects) or the full credit rating process such as a rating committee. The opinions expressed herein are not and should not be represented as a credit rating and should not be taken as an indication of a final credit rating on any particular entity.

Source: S&P Global (China) Ratings.

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Rating Summary

Company Name	Rating Type	Current Rating	Rating Date	Outlook/CreditWatch
Shanghai Rural Commercial Bank Co., Ltd.	Issuer Credit Rating	AAA_{spc}	December 26, 2024	Stable

Stand-alone Credit Profile (SACP)	$aa_{spc}+$	+	External Support	+1	Issuer Credit Rating (ICR)
Anchor	a+		Supporting Entity	Shanghai Municipal Government	AAA_{spc}/Stable
Business Position	0				
Capital & Earnings	0				
Risk Position	+1		Government Support	Very Strong	
Funding & Liquidity	+1				
Holistic Adjustment	+1				

Credit Highlights

Key Strengths	Key Risks
— Very high likelihood of receiving support from the Shanghai government in times of stress.	— Intense banking competition in Shanghai.
— Better asset quality metrics than the industry average, sufficient reserves, and good capital resilience.	— Sustained pressure facing the real estate sector.
— Solid deposit base and a funding structure more stable than the industry average thanks to its primary focus on the local market in Shanghai.	

Surveillance Overview

We monitor the credit quality of SHRCB on a periodic and an ongoing basis. This is periodic surveillance of the bank.

During the surveillance period, SHRCB maintained steady asset expansion and stable business operation. Its capital base is strong and well protected by its adequate reserves. Despite the NIM pressure, its profitability remains sound thanks to effective cost control and stable credit cost. It has a prudent risk appetite and superior asset quality. Its well-established deposit base in Shanghai and limited reliance on wholesale funding have led to more stable funding than the industry average, which helps maintain its solid liquidity metrics.

Our stress testing suggests that risks from real estate sector and local governments' hidden debt have limited impact on the bank's capital adequacy. We estimate it will maintain adequate capital base and decent earnings through the current credit cycle, showing strong capital resilience. Therefore, we raise its SACP from "aa" to "aa+".

Its ICR remained unchanged during the surveillance period as its importance to the Shanghai government stayed the same.

Rating Outlook

The stable outlook reflects our expectation that SHRCB's operational and financial strengths will remain stable, and its importance to the government will remain unchanged over the next two years or beyond.

Downside Scenario: We may consider lowering its ICR if its importance to the government declines significantly. We view this circumstance as highly unlikely to occur in the foreseeable future. We may consider lowering its SACP if its asset quality deteriorates considerably, its reliance on wholesale funding rises remarkably, or its capital resilience weakens substantially.

Related Methodologies, Models & Research

Methodology Applied:

— S&P Global (China) Ratings Financial Institutions Methodology, March 26, 2024.

— S&P Global (China) Ratings General Considerations on Rating Modifiers and Relative Ranking, May 21, 2019.

Model Applied: None.

Peer Comparison

	2022			2023		
	SHRCB	Commercial Bank Average	Rural Bank Average	SHRCB	Commercial Bank Average	Rural Bank Average
Total assets (bil.)	1,281.40	176.79	316.26	1,392.21	196.05	346.53
Net income (bil.)	11.39	1.27	2.25	12.49	1.31	2.34
Reported regulatory capital adequacy ratio (%)	15.46	15.17	12.37	15.74	15.06	12.22
Return on average assets (%)	0.93	0.76	0.53	0.93	0.70	0.54
Non-performing loan ratio (%)	0.94	1.63	3.22	0.97	1.59	3.34
Reserve coverage ratio (%)	445.32	205.85	143.23	404.98	205.14	134.37

Sources: Public information of banks, NAFR, collected and adjusted by S&P Global (China) Ratings.

Note: For rural bank average, total assets and net income are the average of the 50 largest rural banks by asset scale and other metrics are based on the data published by the NAFR.

Anchor

Macro-Economic and Industry Trends

We expect China's GDP growth to slow down in 2025 compared to last year's. In our view, the government's ongoing monetary and fiscal policies will support the real estate sector, the resolution of local government debts, and economic growth. However, a slowing global demand and the uncertainty over new government policies in the U.S. would bring more risks to China's economy. In particular, exports may be hit by higher tariff of the U.S. and subsequently impact investment and consumer sectors.

Considering the economic risk and industry risk faced by China's commercial banking industry, we apply an anchor of "a+" to commercial banks in China.

We expect the overall credit outlook for commercial banks in China to remain stable because of ongoing government support. China's commercial banking sector continues to report stable capital and asset quality metrics, but we continue to expect pressure on credit cost and profitability going forward. State-owned mega banks are expected to maintain stable capitalization and resilient profitability, while small- and medium-sized banks face more pressure. Therefore, we believe the SACPs of commercial banks are likely to show greater differentiation in the foreseeable future. Certain regional banks have weak capital positions, and their asset quality and profitability are sensitive to real estate and LGFV risks. Meanwhile, China's banking sector maintains stable funding and sound liquidity, which wins time for the risk-ridden small- and medium-sized banks to mitigate such risks.

In our opinion, ongoing strong regulatory and government support should keep overall credit quality of the banking sector stable. Considering the economic risk and industry risk faced by China's commercial banking industry, we apply an anchor of "a+" to SHRCB.

Stand-alone Credit Profile

Based in one of China's most developed regions, SHRCB is one of the leading rural commercial banks in China. It was incorporated in 2005 through the merger of 234 rural credit cooperatives in Shanghai. As of the end of June 2024, the bank reported total assets of 1.45 trillion RMB, gross loans of 0.74 trillion RMB, and customer deposits of 1.05 trillion RMB. In 2023, it generated an operating income of 26.41 billion RMB and net income of 12.49 billion RMB, with a return on average equity (ROAE) of 11.25%. As of the end of June 2024, state-owned enterprises held about 60% of the bank's equity. We think the Shanghai government has very strong ability and willingness to support the bank.

Based in one of the most developed regions in China, SHRCB is one of China's largest rural commercial banks.

Business Position

SHRCB is one of China's largest rural commercial banks, with an asset size comparable to major Chinese banks. As of the end of 2023, the bank had a market share nationwide of 0.4% in terms of its total assets, and loan and deposit books, respectively.

The bank's loans and deposits primarily come from Shanghai, where it maintains significant market share. By the end of 2023, the market shares of its loan and deposit books both ranked sixth in Shanghai.

With a national market share of 0.4%, the bank has an average asset size compared with major Chinese banks.

There is no notching adjustment for its business position.

Table 1

SHRCB -- Market Share

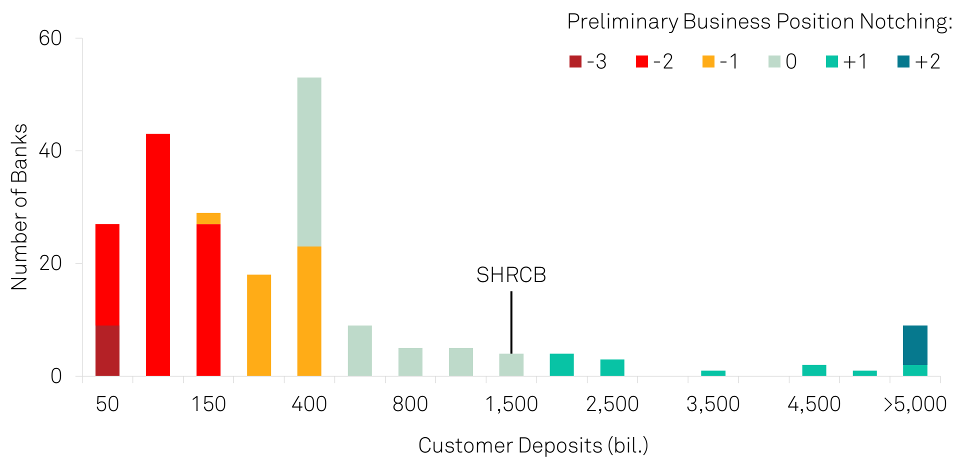
(%)	2020	2021	2022	2023	2024.06
Total assets / total assets of China's commercial banking industry	0.40	0.40	0.40	0.39	0.39
Gross customer loans / total loans of China's commercial banking industry	0.36	0.37	0.37	0.35	0.34
Customer deposits / total deposits of China's commercial banking industry	0.35	0.36	0.36	0.35	0.35
Gross customer loans / total loans of financial institution denominated in local and foreign currencies in Shanghai	6.27	6.39	6.50	6.37	6.21
Gross customer deposits / total deposits of financial institution denominated in local and foreign currencies in Shanghai	4.90	4.86	5.00	4.97	4.92

Sources: SHRCB, NAFR, PBOC, Shanghai Statistical Bulletin, collected and adjusted by S&P Global (China) Ratings.

Chart 1

SHRCB's Business Scale is on Par with the Industry Average

Industry Comparison: Distribution of Deposit Sizes of 200 Major Banks in China as of End of 2023



Sources: Public information of banks, S&P Global (China) Ratings.

SHRCB has an extensive network in Shanghai, enjoying competitive franchise and well-established customer base for its deposit business. As of the end of June 2024, the bank had 365 outlets, 358 of which were in Shanghai and had good coverage over local villages and townships in Shanghai.

In the face of intense competition among banks, SHRCB is looking to gain a competitive edge through differentiation and has set out and implemented a clear strategy accordingly. The bank plans to strengthen its advantages in providing financial services catering to the needs of agriculture, rural areas and farmers in Shanghai and Yangtze River Delta regions and scales up support for promoting rural revitalization, urban and rural integration, and green and low-carbon development in the agricultural sector. As of the end of 2023, the bank's inclusive microloans and agricultural loans accounted for around 10% of its total loan book, respectively.

SHRCB's business is primarily traditional banking. As of the end of 2023, about 58% of its loans were corporate loans, 30% retail loans and the rest trade bills. Given the soft retail loan demand in recent years, the bank's loan growth was primarily driven by corporate lending in 2023. The proportion of retail loans in its loan book decreased from 31.89% by the end of 2022 to 29.65% by the end of 2023.

The decline in the share of retail loans was led by slowing mortgage growth amid residents' reluctance to buy homes. As of the end of June 2024, its mortgages amounted to 103.3 billion RMB, decreasing by 3.05% compared to the beginning of the year and accounting for 14.04% of its loan book, down by 0.94 percentage point compared to the beginning of the year.

In the context of shrinking NIM among banks, SHRCB has seen its operating income grow at a slower pace but still faster than the industry average. In 2023, its operating income came to 26.41 billion RMB, representing a YoY growth of 3.07% versus listed banks' average of 0.70%. Its milder decline in operating income was attributable to smaller NIM contraction and a surge in investment returns in 2023.

Its net interest income has shown a downward trend in recent years. In 2023, its net interest income dropped by 0.26% YoY, compared to a decrease of 1.53% for listed banks. The continued NIM pressure may cause the bank's net interest income to edge down further in 2024. In the first half of 2024, its net interest income reduced by 2.61% YoY to 10.18 billion RMB and operating income rose by 0.23% YoY to 13.92 billion RMB.

The decline in its interest income is mainly due to the weaker performance of its corporate lending segment. In 2023, the average return on its retail loans improved by 0.02 percentage point YoY to 5.24%, while its corporate loans yielded an average of 4.15%, down by 0.47 percentage point YoY.

It maintains a balanced revenue structure. In 2023, corporate banking contributed 49.96% of its total revenue (down by 1.16 percentage points due to decreasing interest rates for corporate loans), retail banking 38.69% (up by 3.70 percentage points YoY), and financial markets 10.90%.

Besides its core business in Shanghai, SHRCB owns several village and township banks. These village and township banks are less profitable than the main operations in Shanghai. As of the end of 2023, it had 35 village and township banks located in Shanghai, Beijing, Shenzhen, Shandong, Hunan, and Yunnan. As of the end of 2023, these village and township banks had total assets of 36.08 billion RMB and net profit of 81 million RMB, accounting for 2.59% and 0.65% of SHRCB's consolidated assets and net profit, respectively.

It holds a 54.29% stake in Yangtze United Financial Leasing, a consolidated subsidiary of the bank. Yangtze United Financial Leasing has decent profitability. As of the end of 2023, the subsidiary's total assets were 37.82 billion RMB, making up 2.72% of the bank's consolidated assets. In 2023, its net profit was 645 million RMB, accounting for 5.17% of the bank's consolidated net profit.

Capital and Earnings

SHRCB has adequate capitalization and healthy profitability, leading to good capital resilience.

Therefore, there is no notching adjustment for capital and earnings.

SHRCB comfortably meets regulatorily required metrics on capital. As of the end of 2023, its reported capital adequacy ratio and tier 1 capital adequacy ratio were 15.74% and 13.35% respectively, much higher the minimum regulatory requirements of 10.5% and 8.5%.

Table 2

SHRCB -- Reported Capital Adequacy Ratios and Capital Quality Metrics (As of End of June 2024)

Metrics (%)	Minimum regulatory requirement	Industry Average	SHRCB
Capital adequacy ratio	10.5	15.53	17.15
Tier 1 capital adequacy ratio	8.5	12.38	14.71
CET 1 capital adequacy ratio	7.5	10.74	14.68
CET 1 capital/net capital	N/A	69.17	85.59
Tier 1 capital/net capital	N/A	79.71	85.79

Sources: SHRCB, NAFR, collected and adjusted by S&P Global (China) Ratings.

The implementation of the Administrative Measures for Commercial Banks' Capital ("the new Measures") has led to a rise in the bank's capital adequacy. The new Measures has come into effect from January 2024. As of the end of June 2024, its reported capital adequacy ratio and tier 1 capital adequacy ratio increased by 1.41 percentage points YoY and 1.37 percentage points YoY to 17.15% and 14.71%, respectively in compliance with the new Measures. Another reason driving the improvement was the less capital consumed in the first half of 2024.

Table 3

SHRCB -- Capital Adequacy Forecast by S&P Global (China) Ratings

<table>
<tr><th rowspan="2">(bil. RMB)</th><th colspan="2">2024 F</th><th colspan="2">2025 F</th><th>Base case assumptions and conclusions</th></tr>
<tr><th>Amount</th><th>YoY Change</th><th>Amount</th><th>YoY Change</th><td>We expect the bank's RWA to remain flat YoY in 2024 and grow by 5% in 2025, given the impact of the new Measures on RWA.</td></tr>
<tr><td>Risk-weighted assets</td><td>846</td><td>0%</td><td>889</td><td>5%</td><td>The bank's NIM is expected to be around 1.5% in 2024 and 2025.</td></tr>
<tr><td>Tier 1 capital</td><td>122</td><td>8%</td><td>131</td><td>7%</td><td>We expect the bank to maintain its cost-to-income ratio at about 30% and reserve-to-loan ratio at around 3.6%.
Given the above assumptions, the bank's ROAE is estimated to be about 10% in 2024 and 2025.
We assume a dividend payout ratio of 30% and expect no material capital injection from external sources and no perpetual bonds to be issued in 2024.
Considering the bank's profit, dividend and capital plan, we project its tier 1 capital to grow by 7-8% YoY in 2024 and 2025, which should meet its capital needs for supporting RWA growth.</td></tr>
<tr><td>Tier 1 capital adequacy ratio forecast</td><td colspan="2">About 14%</td><td colspan="2">About 14%</td><td>We expect the bank's tier 1 capital adequacy ratio to stay around 14% in 2024 and 2025, indicating very strong capital base.</td></tr>
</table>

Note: F – Forecast.
Source: S&P Global (China) Ratings.

The bank's outstanding asset quality, adequate reserves, and healthy profitability ensure its strong capitalization in times of stress. Our stress test shows that the bank demonstrates stronger capital resilience than its peers under stress scenarios. We think the bank can maintain healthy capital strengths even if the broad environment becomes increasingly uncertain in the future.

Table 4

Capital Stress Testing on SHRCB by S&P Global (China) Ratings (Based on data as of end of June 2024)

Scenarios	Tier 1 Capital Adequacy Ratio (%)
Reported ratio	14.71
Key assumptions under baseline stress scenario: 1. Problem loan ratio for real estate loans and construction loans is 15%, with a loss rate of 50%. 2. Problem loan ratio for mortgages is 1%, with a loss rate of 10%. 3. Problem loan ratio for other loans is 7%, with a loss rate of 70%. 4. Stage 2 and stage 3 investment assets are problem assets, with a loss rate of 70%. 5. Interest rate for weak LGFVs decreases by 100-200 basis points. 6. Spreads between LPR and deposit rates remain flat as in 2023. 7. Average mortgage rate drops by 73 basis points in 2024 due to basis-point cuts to interest rates for outstanding mortgages in the second half of 2023. 8. 30% of problem loans and investment assets cease interest payment. 9. Cash recovery rate for foreclosed assets (excl. assets assigned with 1250% risk weight as per regulatory capital requirements) uncovered by loss reserves is 30%.	14.71
Key assumptions under adverse stress scenario: 1. Problem loan ratio for real estate loans and construction loans is 30%, with a loss rate of 70%. 2. Problem loan ratio for mortgages is 2%, with a loss rate of 20%. 3. Interest rate for weak LGFVs decreases by 200-300 basis points. 4. Spreads between LPR and deposit rates narrow by 10 basis points from 2023. 5. Other assumptions are same as baseline stress scenario.	14.40
Key assumptions under severe adverse stress scenario: 1. Problem loan ratio for real estate loans and construction loans is 50%, with a loss rate of 70%. 2. Problem loan ratio for mortgages is 3%, with a loss rate of 30%. 3. Interest rate for weak LGFVs decreases by 300-400 basis points. 4. Spreads between LPR and deposit rates narrow by 20 basis points from 2023. 5. Other assumptions are same as baseline stress scenario.	12.30
Main conclusion: The bank has very resilient capital base and could maintain healthy capital adequacy under severe adverse stress.	

Note: This stress testing didn't factor in growth in RWA led by business expansion.

Source: S&P Global (China) Ratings.

China's commercial banking industry has seen downward NIM pressure in recent years, which has been primarily driven by several rounds of LPR cuts, downward adjustments to interest rates of outstanding mortgages, lower interest rates for local governments' exposure to hidden debts, and increasing migration toward term deposits among banks. The commercial banking industry's average NIM decreased by 22bps YoY to 1.69% in 2023 and dropped by 20bps YoY to 1.54% in the first half of 2024.

Due to changes in market rates, the bank's NIM has narrowed. It reported a NIM of 1.67% in 2023, down by 16bps from the previous year. In the first half of 2024, its NIM dropped by 16bps YoY to 1.56%. We expect its NIM decline throughout 2024 to range from 15-20 basis points.

Its NIM compression in 2024 has largely resulted from asset-side changes, partially due to LPR cuts and partially the lowering of interest rates of outstanding mortgages. According to the PBOC Shanghai branch, the interest rates of outstanding mortgages in Shanghai went down by roughly 54 basis points on average following the one-off LPR cut in the second half of 2023. In addition, the over-five-year LPR has been adjusted down by 35 basis points in aggregate 2024 to date, which would have a material impact on new mortgages issued within the year.

Its NIM decline is milder than the industry average. This is because the bank has maintained effective control on its liabilities. In 2023, the average cost for its deposits decreased by 6 basis points YoY to 1.95%. In addition, its modest exposure to LGFVs makes its loan rates less impacted by LGFV debt-relieving measures compared to many other regional banks. Its LGFV exposure represents a very small share of gross loans and is distributed in Shanghai and developed regions in the vicinity. We expect domestic banks to face a NIM shrinkage of about 5 basis points following the implementation of debt-relieving measures in 2024, compared to a NIM contraction of less than 1 basis point for the bank due to the same impact.

Thanks to its good asset quality and adequate reserves, SHRCB's credit cost is significantly lower than its peers. In 2023, the bank's credit cost (current loan provisioning/average gross loans) was 0.33% (compared to listed banks' average of about 0.8%), and provisioning cost as a percentage of pre-provision profit was 18.35% (compared to listed banks' average of roughly 34%). In the first half of 2024, the bank's provisioning cost accounted for 11.14% of pre-provisioning profit, 7.2 percentage points lower than that in 2023.

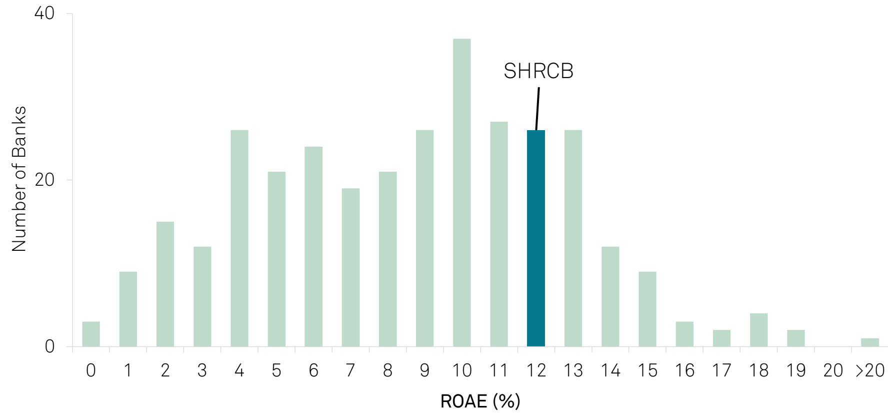
The bank maintains effective control on operating costs. In 2023, its reported cost-to-income ratio was 32.67%, below the industry average of 35.26%. In the first half of 2024, this ratio stood at 29.11%, versus the industry average of 30.71%.

Due to the effective control on credit and operating costs, the bank has seen healthy profitability. In 2023, its net income increased by 9.60% YoY to 12.49 billion RMB with a ROAE of 11.34%, higher than the industry average of 8.93%. In the first half of 2024, the bank reported a net income of 7.14 billion RMB, generally flat compared to the same period last year and with an annualized ROAE of 11.89%. We think its profitability will continue to stand better than the industry average due to its asset quality strength.

Chart 2

SHRCB's Profitability Remains Robust

Industry Comparison: ROAE of Major Banks in China in 2023



Sources: Public information of banks, collected and adjusted by S&P Global (China) Ratings.

Risk Position

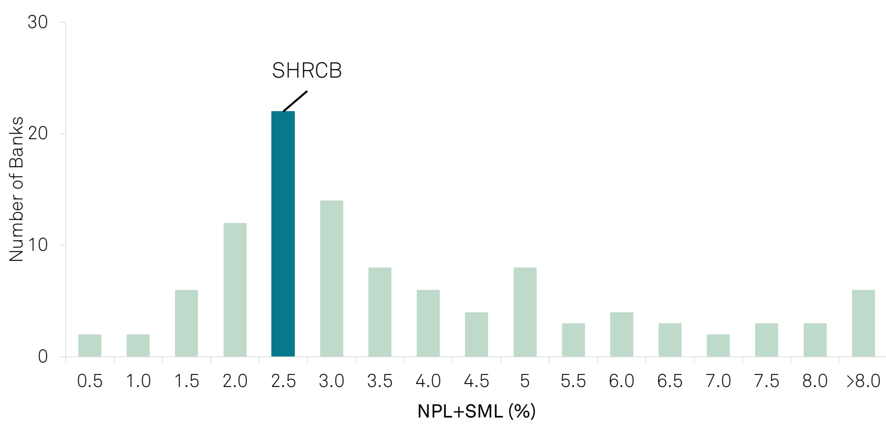
Thanks to the good credit environment in Shanghai and the bank's prudent approach to risk management and operations, SHRCB has maintained its asset quality metrics above industry average. As of the end of 2023, its NPL ratio was 0.97%, lower than the industry average of 1.59%. Its SML accounted for 1.23% of its gross loans, significantly lower than the industry average of 2.20%. Its modest bad debt size leads to its low net write-off rate, which came at 0.36% in 2023 and averaged 0.21% for 2019-2023, compared to the industry average of over 0.5%.

Thanks to the good credit environment in Shanghai and the bank's prudent risk management, SHRCB's asset quality metrics are above the industry average. As such, there is one-notch uplift to its risk position.

Chart 3

SHRCB's Assets Quality is Better than Industry Average

Industry Comparison: Distribution of NPL+SML Ratios of Major Banks in China as of End of 2023



Sources: Public information of banks, S&P Global (China) Ratings.

We view the bank's loan classification practice as disciplined and prudent. As of the end of 2023, the ratio of 90+ DPD loans to NPLs was 94%. Its overdue loan ratio has remained stable for years, staying at 1.25% as of the end of 2023 and 1.25% on average from 2019 to 2023.

The bank's exposure to refinancing loans is controllable. In 2023, it issued "SME-focused rollover loans" of 61.2 billion RMB in aggregate, in which refinancing loans for SMEs totaled 20.0 billion RMB. These loans, given their very small scale, would not bring a materially negative impact on the bank's asset quality.

It has relatively high exposure to real estate sector, but the credit risk remains under control. As of the end of 2023, its real estate loans accounted for 14.71% of its loan book, down by 0.27 percentage point from the previous year. The NPL ratio of real estate loans was 2.18%, versus listed banks' average of 3.52%. Its construction loans accounted for 1.60% of its loan book with an NPL ratio of 1.19%, compared to listed banks' average of 1.43%. The bank's real estate loans are primarily located in Shanghai. Considering the resilient property market in Shanghai and the bank's reinforced management in the flow of funds toward real estate projects, we view the bank's credit risk related to real estate sector as generally controllable. Our stress testing suggests that the bank enjoys a buffer through its adequate reserves, earnings, and capital resilience in the face of property sector pressure (see Table 3 for details).

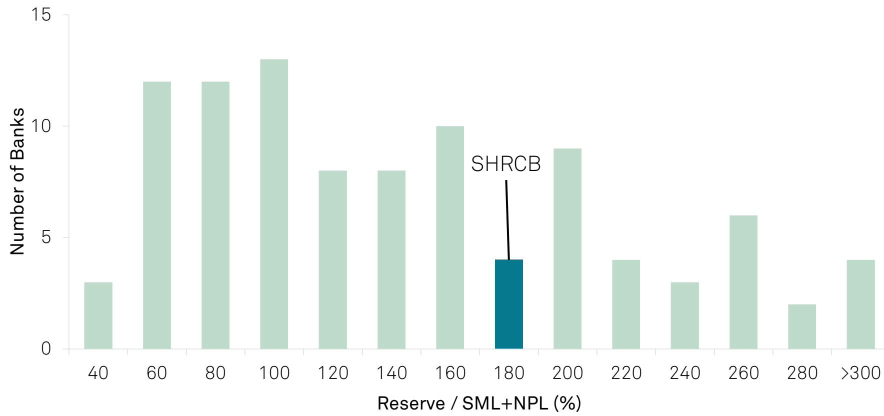
More than 90% of its loans are located in Shanghai, where the well-developed and diversified economy has significantly mitigated its concentration risk as a regional bank. The Shanghai government's fiscal position is very strong with minimal exposure to hidden debt and almost no exposure to high-risk LGFVs. We believe the bank sees significantly lower LGFV risk compared to regional banks' average.

The bank has a reserve buffer high enough to absorb asset quality uncertainty and maintain its resilient profitability and capitalization. As of the end of June 2024, its reserve coverage ratio was 372.42%, far above the rural commercial bank average of 143.14% and the overall commercial bank average of 209.32%. Its loan loss reserves' coverage of NPLs plus SMLs was 164.41%, sufficient to absorb any stress from SML loan migration. Assuming a reasonable recovery rate, the bank's reserves could fully cover potential problem loans and protect its capital against bad debt erosion, while at the same time underpinning its healthy profitability.

Chart 4

The Bank's Reserve Coverage of Problem Loans is Much Higher than Industry Average Level

Industry Comparison: Distribution of Loan Loss Reserve/(NPL+SML) of Major Banks in China as of End of 2023



Sources: Public information of banks, collected and adjusted by S&P Global (China) Ratings.

The bank adopts prudent approach to asset allocation, which leads to sound asset quality of its investment portfolio. As of the end of 2023, financial institution bonds (including NCDs) accounted for roughly 51% of its investment portfolio, government bonds 32%, corporate bonds 14%, and non-standard products 2%. Meanwhile, stage 2 and stage 3 assets accounted for less than 0.1% of financial investments, demonstrating very low credit risk.

Funding and Liquidity

SHRCB has a solid deposit base, a prominent share of retail loans, limited use of wholesale funding, and more stable funding than the industry average. Its good funding position is attributed to its vast deposit network in the suburban and rural areas of Shanghai. As of the end of 2023, 80% of its total liabilities were customer deposits. Specifically, retail deposits amounted to 532.57 billion RMB, accounting for 52% of customer deposits. In addition, its close relationship with local companies and institutions has also led to high stickiness of its corporate loans.

The bank has a solid deposit base in Shanghai, and a low reliance on wholesale funding, indicating a more stable funding than the industry average. It also maintains very good liquidity metrics.

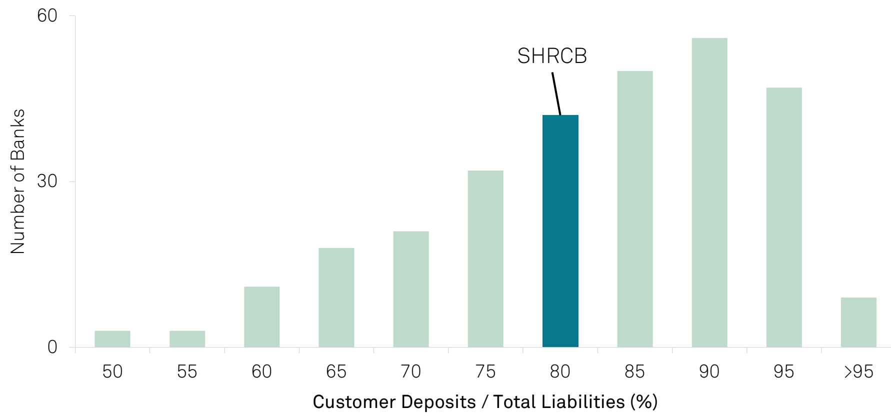
Therefore, we apply a one-notch uplift to its funding and liquidity.

The bank has seen rapid growth in retail deposits amid decreasing risk appetite among retail customers and their rising desire for deposits as a safer investment. Its retail deposits grew by 11.90% YoY as of the end of 2023 and their share in customer deposits rose to over 52% by the end of June 2024 from less than 48% by the end of 2020.

Chart 5

The Bank has Limited Reliance on Wholesale Funding

Industry Comparison: Distribution of Customer Loans/Total Liabilities of 200 Major Banks in China as of End of 2023



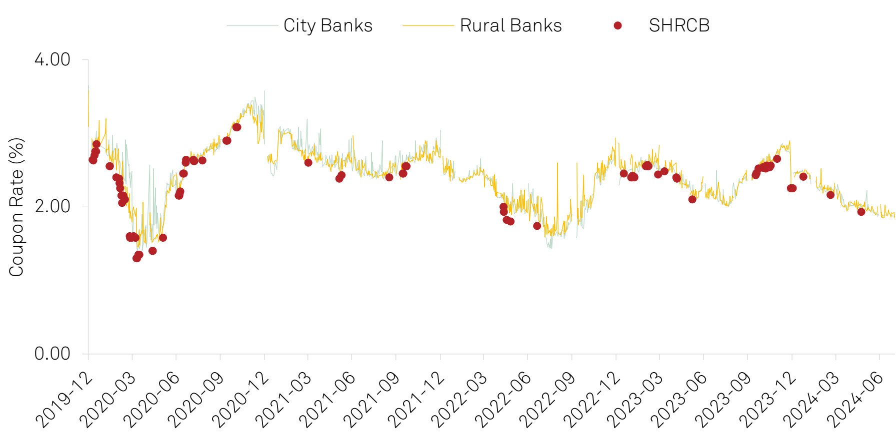
Sources: Public information of banks, collected and adjusted by S&P Global (China) Ratings.

Based on observed market data, its credit spread for wholesale funding is low compared with other commercial banks. In our view, its low funding cost reflects its easy access to funding in the interbank market thanks to its status as one of the top rural banks in China.

Chart 6

SHRCB Enjoys a Wholesale Funding Cost Lower than Regional Bank Average

Industry Comparison: Issue Rates of 3-month NCDs of Regional Banks



Source: Wind, collected and adjusted by S&P Global (China) Ratings.

We assess the bank's liquidity position as strong, with liquidity metrics better than the industry average. As of the end of June 2024, its liquidity coverage ratio was 166.43%, far above the minimum regulatory requirement of 100% and the industry average of 150.70%. Its net stable funding ratio was 135.10%, higher than the minimum regulatory requirement of 100% and the industry average of 125.92%.

Holistic Adjustment

We apply a one-notch upward holistic adjustment to the bank's SACP through peer comparison to comprehensively reflect its strengths in stand-alone credit quality. The one-notch upward holistic adjustment is reflective of its credit strengths listed below that are not fully captured by assessments on the four credit risk factors above：

- Stable business franchise given its status as one of the largest rural banks in China. It has extensive network and a solid customer base in Shanghai. As of the end of June 2024, its total assets reached 1.45 trillion RMB.
- Superior asset quality and adequate reserves, with very high capital adequacy to address risks associated with real estate and local governments' debt. We anticipate its tier 1 capital adequacy ratio will comfortably meet the minimum regulatory requirement in times of severe adverse stress (see Table 3).
- Stronger profitability than the industry average. It has delivered an ROAE of 11.50% over the past five years (2019-2023), better than an average of 9.67% for its peers during the same period. We expect the bank to continue to generate decent earnings because of its very good asset quality.

We apply a one-notch upward holistic adjustment to the bank. Its SACP of "aa_{spc}+" is three notches higher than the anchor of "a+". This reflects its competitiveness in business stability, capital resilience, profitability, asset quality, and funding and liquidity.

Issuer Credit Rating

External Support

Considering the bank's equity structure and its important role in the local financial market, we think SHRCB has high importance to the Shanghai government. The bank has played an important role in providing financial services to local MSEs and the local agriculture sector, and owns a significant market share in Shanghai. The bank is a state-owned regional rural commercial bank and has close relationship with the Shanghai government. As of the end of 2023, about 60% of the bank's equity was held by state-owned entities, in which 9.99% was held by Shanghai State-owned Assets Management Co., Ltd. and its related and concert parties —Shanghai International Group Co., Ltd. and Shanghai International Group Asset Management Co., Ltd.

SHRCB has a significant market share in Shanghai and has high importance to the Shanghai government.

Given the Shanghai government's strong ability and willingness to provide support, we give it a one-notch uplift for government support to arrive at its ICR of AAA_{spc}.

Table 5

SHRCB: 10 Largest Shareholder, End of 2023

Shareholder Name	Holding (%)
Shanghai State-owned Assets Management Co., Ltd	9.29
China COSCO Shipping Corporation Limited	8.29
Baoshan Iron & Steel Co., Ltd	8.29
Shanghai Jiushi (Group) Co., Ltd	7.72
China Pacific Life Insurance Co., Ltd	5.81
Shanghai Guosheng Group Assets Co., Ltd	4.97
Zhejiang Expressway Co., Ltd	4.92
China Taiping Life Insurance Co., Ltd	4.30
Shanghai Shendi (Group) Co., Ltd	3.71
Lanhai Holdings (Group) Co., Ltd	3.48
Total	**60.78**

Source: SHRCB, collected and adjusted by S&P Global (China) Ratings.

The Shanghai government plays an important role in the management of SHRCB. The senior management of SHRCB are recommended by the Shanghai government and approved by the NAFR. The senior management of the bank is also subject to performance evaluation by the Shanghai government.

Given the high likelihood of government support and the strong support ability of the Shanghai government, we assign an ICR of "AAA_{spc}" to SHRCB, representing a one-notch uplift from its SACP of "$\text{aa}_{\text{spc}}+$".

Appendix

Appendix 1: Key Financial Data

SHRCB: Key Financial Data and Ratios

	2020	2021	2022	2023	2024.06/H1
Business Position					
Total assets (bil.)	1,056.98	1,158.38	1,281.40	1,392.21	1,454.96
Total assets YoY growth (%)	13.66	9.59	10.62	8.65	N/A
Customer loans (bil.)	530.67	613.58	670.62	711.48	735.88
Customer loans YoY growth (%)	13.67	15.62	9.30	6.09	N/A
Customer deposits (bil.)	748.99	838.14	943.48	1,016.41	1,047.39
Customer deposits YoY growth (%)	8.18	11.90	12.57	7.73	N/A
Operating income (bil.)	22.04	24.16	25.63	26.41	13.92
Operating income YoY growth (%)	3.61	9.64	6.05	3.07	N/A
Net income (bil.)	8.42	10.05	11.39	12.49	7.14
Net income YoY growth (%)	(5.82)	19.34	13.40	9.60	N/A
Net fees and commission income/operating income (%)	10.58	8.96	8.41	8.59	8.95
Capital and Earnings					
Reported regulatory capital adequacy ratio (%)	14.40	15.28	15.46	15.74	17.15
Reported regulatory Tier 1 capital adequacy ratio (%)	11.70	13.10	12.99	13.35	14.71
Adjusted net interest margin (%)	1.91	1.87	1.80	1.64	N/A
Cost-to-income ratio (%)	28.78	29.89	30.43	32.56	29.06
Asset provisioning/pre-provision operating profits (%)	36.32	26.99	22.04	18.35	11.14
Loan provisioning/average gross customer loans (%)	0.99	0.76	0.52	0.33	N/A
Return on average assets (%)	0.85	0.91	0.93	0.93	N/A
Return on average equity (%)	10.89	11.30	11.22	11.25	N/A
Risk Position					
Non-performing loan ratio (%)	0.99	0.95	0.94	0.97	0.97
(Non-performing loans + special mention loans) /gross customer loans (%)	1.75	1.42	1.69	2.21	2.19
Loan loss reserve/gross customer loans (%)	4.14	4.20	4.21	3.94	3.61
Reserve coverage ratio (%)	419.17	442.50	445.32	404.98	372.42
Loan loss reserve/ (non-performing loans + special mention loans) (%)	236.67	296.94	249.67	178.65	164.41
Net write-off amount/ average customer loans (%)	0.23	0.10	0.14	0.36	N/A
Funding and Liquidity					
Customer loans/customer deposits (%)	70.85	73.21	71.08	70.00	70.26
Customer deposits/total liabilities (%)	76.70	78.99	80.25	79.67	78.60
Wholesale funding /total liabilities (%)	20.78	18.27	16.54	17.71	18.76
Retail deposits/customer deposits (%)	47.90	47.96	50.44	52.40	53.24
Liquidity coverage ratio (%)	265.58	247.65	253.71	189.20	166.43

Note 1: We believe that SHRCB has a clear business model and strict financial management, and we have not made significant adjustments to the bank's financial data.

Note 2: The bank's 2019-2021 financial statements were audited by Deloitte China and its 2022-2023 financial statements were audited by KPMG China. All these financial statements were assigned with standard unqualified opinions. Its 2024 H1 financial data were reviewed by KPMG China.

Note 3: Accrued interest has been excluded from gross loans and customer deposits since 2020.

Note 4: Adjusted net interest margin (%) = Net Interest Income/ [(total interest-bearing assets at the beginning of the year +total interest-bearing assets as of the end of the year)/2].

Note 5: Cost-to-income ratio = business and management fees/operating income.

Note 6: Return on average assets =net income/ [(total assets at the beginning of the year +total assets as of the end of the year)/2].

Note 7: Return on average equity =net income/ [(total equity at the beginning of the year +total equity as of the end of the year)/2].

Note 8: Wholesale funding=borrowing from the central bank + borrowing and deposits from other financial institutions + financial assets sold for repurchase + financial liabilities held for trading + bonds payable.

Source: SHRCB, collected and adjusted by S&P Global (China) Ratings.

Appendix 2: Rating History of SHRCB by S&P Global (China) Ratings

Issuer Credit Ratings	Outlook/CreditWatch	Rating Date	Analysts	Related Reports
AA_{spc}-	Stable	2020-01-14	Yifu Wang, Xiaochen Luan, Cong Cui	Credit Rating Report: Shanghai Rural Commercial Bank Co., Ltd., January 14, 2020
AA_{spc}-	Stable	2021-03-15	Yifu Wang, Xiaochen Luan, Cong Cui	Credit Rating Report: Shanghai Rural Commercial Bank Co., Ltd., March 17, 2021
AA_{spc}-	Stable	2022-03-15	Longtai Chen, Xiaochen Luan, Cong Cui	Credit Rating Report: Shanghai Rural Commercial Bank Co., Ltd., March 15, 2022
AA_{spc}-	Stable	2023-03-15	Xiaochen Luan, Jiancheng Yang, Jiachuan Xu	Credit Rating Report: Shanghai Rural Commercial Bank Co., Ltd., March 15, 2023
AAA_{spc}	Stable	2024-01-10	Xiaochen Luan, Jiancheng Yang, Jiachuan Xu	Credit Rating Report: Shanghai Rural Commercial Bank Co., Ltd., January 10, 2024
AAA_{spc}	Stable	2024-12-26	Xuefei Zou, Jiachuan Xu	Current Report

Note: These ratings are conducted based on S&P Global (China) Ratings Financial Institutions Methodology, and no quantitative model is used. S&P Global (China) Ratings revised its financial institutions methodology in December 2023. The rating committee has reviewed the bank according to the revised methodology, which has led to an upgrade to the bank's ICR in January 2024.

Appendix 3: Ratings Definitions

Category	Definition
AAA_{spc}	The repayment ability is extremely strong, generally not impacted by any adverse economic environment, and the default risk is extremely low.
AA_{spc}	The repayment ability is very strong, not considerably impacted by any adverse economic environment, and the default risk is very low.
A_{spc}	The repayment ability is comparatively strong, comparatively vulnerable to the impact of adverse economic environment, and the default risk is comparatively low.
BBB_{spc}	The repayment ability is average, comparatively impacted by adverse economic environment, and the default risk is average.
BB_{spc}	The repayment ability is comparatively weak, materially impacted by adverse economic environment, and the default risk is comparatively high.
B_{spc}	The repayment ability relies comparatively on fair economic environment and the default risk is very high.
CCC_{spc}	The repayment ability relies extremely on fair economic environment and the default risk is extremely high.
CC_{spc}	Lower protection in situation of bankruptcy or reorganization and the repayment of debt may not be generally guaranteed.
C_{spc}	Unable to repay the debt.

Note: Except for AAA_{spc} and ratings below CCC_{spc}, each rating may be added a "+" or "-" sign for minor adjustment to indicate a slightly higher or lower rating.

Appendix 4: Surveillance Plan

S&P Ratings (China) Co., Ltd. shall monitor the credit quality of the rated issuer on a periodic (if applicable) and an ongoing basis. If any material credit events are likely to change the credit quality of the issuer, we will conduct ad-hoc surveillance, and determine whether the outstanding ratings need to be adjusted.