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S&P Global
China Ratings

Bulletin:

Luzhou Bank's Credit Quality Remains Stable

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BEIJING, March 30, 2020 – S&P Global (China) Ratings today said that the financial performance of Luzhou Bank Co., Ltd. ("Luzhou Bank", BBB_{spc}/Stable) in 2019 is in line with the rating agency's expectations and the bank's credit quality remains stable.

Luzhou Bank maintained robust business growth in 2019. As of the end of 2019, the bank reported total assets of 91.7 billion RMB, up by 11% YoY, lower than the industry average growth rate of 14% but higher than the city bank sub-sector average growth of 9%. Its loan book grew at a much faster pace. As of the end of 2019, Luzhou Bank's loan book was 44.8 billion RMB, up by 43% YoY. The bank reported an operating revenue of 2.8 billion RMB in 2019, up by 45% YoY.

We expect Luzhou Bank to maintain adequate capital adequacy ratios. As of the end of 2019, it reported a tier-1 capital adequacy ratio of 9.31% and a total capital adequacy ratio of 12.09%, above the minimum regulatory requirements. In addition, the bank issued 1 billion RMB of additional tier-1 capital bonds in March 2020. The bank also has plans to raise new equity and issue tier-2 capital bonds, which would further solidify its capital base.

Affected by asset quality pressure, Luzhou Bank's profitability in 2019 was lower than that of 2018 and was in line with the industry average. Thanks to the rapid growth of its loan book, its net interest margin increased from 2.53% in 2018 to 3.08% in 2019, a level significantly higher than the industry average of 2.20%. However, due to increasing bad debts, Luzhou Bank's impairment charge rose by 138% YoY and accounted for 34% of its operating revenue. As a result, the bank reported net income of 634 million RMB in 2019, down by 3.7% YoY. Its return on average assets was 0.73% in 2019, in line with the average profitability level of city banks in China.

Luzhou Bank's asset quality is consistent with the industry average in China. As of the end of 2019, the bank's non-performing loan ("NPL") ratio was 0.94%, 0.92 percentage points lower than the industry average, and its special mention loan ("SML") ratio was 3.66%, higher than the industry average of 2.91%. Its overdue loans accounted for 1.48% of its total loans. The bank's asset quality performance in 2019 is in line with our expectations. As economic growth slows down in China, we expect increasing bad debt challenges for China's small and mid-sized city banks.

We expect Luzhou Bank's provisioning cost to remain high in 2020. As of the end of 2019, its loan loss reserve was 350% of its NPLs and 71% of its NPLs+SMLs. Given the rising uncertainty caused by COVID-19, we expect continuing provision pressure going forward.

This report does not constitute a rating action

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