Credit Rating Announcement

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ICBC – Ratings Affirmed with a Stable Outlook

Capital Intelligence Ratings (CI Ratings or CI) today announced that it has affirmed the Long-Term Foreign Currency Rating (LT FCR) and Short-Term Foreign Currency Rating (ST FCR) of Industrial and Commercial Bank of China (ICBC) at 'A' and 'A1', respectively. At the same time, CI Ratings has affirmed ICBC's Bank Standalone Rating (BSR) at 'bbb-' and Core Financial Strength (CFS) rating at 'bbb'. The Outlook for the LT FCR and BSR remains Stable.

The four-notch uplift of the LT FCR above the BSR is based on an ESL of Very High. The ESL takes into account ICBC's majority state-ownership and G-SIB status. Furthermore, the Chinese government has a strong track record of extending assistance to troubled banks in case of need, and ample resources and policy flexibility to support the banking sector as a whole notwithstanding a decline in its fiscal position due to the economic slowdown in recent years. The Bank's LT FCR is aligned with CI's internal assessment of sovereign credit risk for China.

ICBC's BSR is derived from a CFS rating of 'bbb' and an Operating Environment Risk Anchor (OPERA) of 'bbb-', the latter indicating modest risk. OPERA balances the economy's high competitiveness, strong external position and large diversification against very high macro-financial risks, ongoing weaknesses in the property market that is hampering growth, and rising external risk factors in addition to persistent institutional weaknesses. While the current official financial ratios of Chinese banking institutions are satisfactory, CI is concerned that the weak property market and increasing financial stress in the local government financing vehicle (LGFV) sector are increasing the vulnerability of the Chinese banking sector.

The Bank's BSR and CFS rating are supported by comfortable liquidity, supported by a large financial investment portfolio and deep customer deposit base, good and resilient loan asset quality metrics, and solid capital ratios. The main challenge for ICBC, in common with the sector, is the low and declining interest rate environment which is putting pressure on earnings and profitability metrics. Furthermore, the moderate economic growth, headwinds from the prolonged downturn in the real estate sector, and rising financial stress in the LGFV segment are likely to keep credit risk elevated. The main constraint for the Bank's ratings is the significant exposure to the weak real estate market, although overall exposure has declined noticeably over the past two years. That said, exposure comprises mainly good quality residential mortgages. The ratings are further constrained by the lack of disclosure on LGFV exposure which restricts a full assessment of overall asset quality. Financial stress in this segment has also been rising. In this regard, CI continues to draw comfort from the consistently good quality of the Bank's loans and investments to date.

ICBC is the largest bank in the world in terms of total assets at end-Q1 24. The Bank has the most extensive distribution network in the country and a significant and growing overseas presence. Reflecting its strong domestic franchise, its asset base is largely restricted to China with a prudent level of loans. The loan book remains skewed towards the corporate segment, although this exposure is well dispersed across a wide range of economic sectors. Due to the large residential mortgage portfolio, the Bank's real estate concentration risk remains high (despite recent declines). However, housing loans are generally collateralised and granular in nature. Moreover, this concentration risk is mitigated by the good quality of the loan book.

ICBC continued to display good and resilient loan asset quality metrics at end-2023 and Q1 24. The rise in NPLs during this period was largely offset by loan growth. The NPL ratio remained better than the average for the commercial banking sector at end-2023. Reflecting the Bank's proactive provisioning policy, loan loss reserve coverage was further strengthened in both periods and stayed ahead of the commercial banking averages. Stage 2 loans were low despite an increase in 2023, and restructured and overdue loans under 90 days were limited. Going forward, despite the elevated credit risk environment, CI anticipates ICBC to maintain good loan asset quality metrics. The Bank generates a fairly good level of operating profit to support provisioning requirements, and the solid capital base provides additional buffer. As with its peers, the Bank has a sizeable portfolio of financial investments comprising a large proportion in government bonds. The latter has been rising in recent periods to a high level as a percentage of equity.

A key credit strength of ICBC is its deep customer deposit base alongside good customer deposit expansion in 2023, which picked up further in the first three months of 2024. Notwithstanding the declining interest rate environment, time deposits continued to grow as did retail deposits. Wholesale funds remained moderate despite rising in 2023 and Q1 24. A credit negative is the high level of short-term interbank deposits. Refinancing risk is considered moderate given longer term tenor of borrowings, the Bank's ready access to the capital market, and its G-SIB status and position as the largest bank in the world. ICBC's other liquidity metrics relating to liquid asset and net broad liquid asset ratios are also solid, and remain supported by a large portfolio of financial investments comprising government and policy bank bonds. The Bank's good liquidity buffer is also reflected by improving and well above regulatory requirements LCR and NSFR ratios.

Another key strength is the Bank's solid and unimpaired capital base which continued to be replenished internally through retained earnings and via Tier 2 capital issuances. Consequently, capital ratios were largely maintained and stayed ahead of the peer group averages in 2023 and Q1 24. ICBC's total CAR remained higher than that of the reported sector average at end-2023. Internal capital generation however weakened in line with slower earnings growth and the peer group trend. The balance sheet and Basel III leverage ratios inched down further in 2023 and Q1 24 but remained fairly sound.

Following the trend seen in the sector, earnings performance was impacted by low and declining interest rates, as well as the government's request for banks to support the real economy. Net interest income (NII) contracted in 2023 due largely to a further and sizeable narrowing of the net interest margin (NIM) while fee-based income continued to decline, which led to a larger fall in operating income. Consequently, despite good operating efficiency, the Bank's operating profit declined in 2023. However, a further fall in the net impairment charge enabled the Bank to record a marginal increase in net profit. As with many of its peers, ICBC reported a weaker earnings performance for the first three months of 2024. NII contracted further while fee and commission income continued to lag the previous period. An increase in operating expense led to a larger y-o-y decline in operating profit, but a reduction in impairment charges narrowed the y-o-y fall in net profit in Q1 24. ROAA declined in both 2023 and Q1 24 but some improvement was seen in operating profitability in Q1 24.

We expect profitability to remain a key challenge for ICBC going forward (in common with the sector). NIM is likely to remain under pressure following the recent interest rate cut in July of this year. The slower economic growth, alongside stresses in certain economic sectors, could also keep impairment charges elevated. CI thus anticipates the Bank's profitability metrics to remain fairly moderate, although they will probably continue to compare well with the top four commercial banks in the country.

Rating Outlook

The Stable Outlook indicates that the ratings are likely to remain unchanged over the next 12 months. The Outlook balances the challenging operating environment against the Bank's good financial standing in terms of loan asset quality, liquidity, and capital positions.

Rating Dynamics: Upside Scenario

As the LT FCR is in line with CI's internal assessment of China's sovereign risk, the Outlook could be revised to Positive and/or the rating revised upwards if there is similar upward revision of CI's internal assessment of the Chinese government's credit strength. This scenario is however remote at this stage. The Outlook on the Bank's BSR could be revised to Positive and/or the rating revised upwards if there is a significant and sustainable improvement in profitability ratios.

Rating Dynamics: Downside Scenario

Although not our base case, the Outlook on the LT FCR could be revised to Negative or the ratings lowered by one notch if CI revises downwards its internal assessment of the Chinese government's credit strength or its willingness and ability to support the Bank, and/or if there is a downward revision of OPERA. The Outlook on the Bank's BSR could be revised to Negative or the rating lowered by one notch in the next 12 months if the Bank's loan asset quality and profitability weaken substantially.

Ratings

Foreign Currency		Outlook	BSR	Outlook	CFS	ESL	OPERA
LT	ST	LT FC		BSR			
A	A1	Stable	bbb-	Stable	bbb	Very High	bbb-

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About the Ratings

The credit ratings have been issued by Capital Intelligence Ratings Ltd, P.O. Box 53585, Limassol 3303, Cyprus.

The following information source was used to prepare the credit ratings: public information. Financial data and metrics have been derived by CI from the rated entity's financial statements for FY2021-23 and Q1 2024. CI may also have relied upon non-public financial information provided by the rated entity and may also have used financial information from credible, independent third-party data providers. CI considers the quality of information available on the rated entity to be satisfactory for the purposes of assigning and maintaining credit ratings. CI does not audit or independently verify information received during the rating process.

The principal methodology used to determine the ratings is the Bank Rating Methodology, dated 3 April 2019 (see www.ciratings.com/page/rating-methodologies/bank-ratings). Information on rating scales and definitions, the time horizon of rating outlooks, and the definition of default can be found at www.ciratings.com/page/our-policies-procedures. Historical performance data, including default rates, are available from a central repository established by ESMA (CEREP) at http://cerep.esma.europa.eu

This rating action follows a scheduled periodic (annual) review of the rated entity. Ratings on the entity were first released in March 1992. The ratings were last updated in September 2023. The ratings and rating outlook were disclosed to the rated entity prior to publication and were not amended following that disclosure.

The ratings have been initiated by CI. The following scheme is therefore applicable in accordance with EU regulatory guidelines.

<u>Unsolicited Credit Rating</u>

With Rated Entity or Related Third Party Participation:	No
With Access to Internal Documents:	No
With Access to Management:	No

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