

Japan Credit Rating Agency, Ltd. (JCR) announces the following credit rating.

Seto Shinkin Bank (security code: -)

<Affirmation>

Long-term Issuer Rating: A-
Outlook: Stable

Rationale

- (1) Seto Shinkin Bank (the "Bank") is a shinkin bank headquartered in Seto City, Aichi Prefecture with a fund volume of around 2 trillion yen. It stably holds large market shares for deposits and loans in Seto City and also covers Nagoya City and its surrounding area with its strong branch network. These solid business bases and high core capital ratio support its rating. The Bank's earnings capacity significantly dropped in the fiscal year ended March 2017 (FY2016) after the Bank of Japan's introduction of negative interest rate policy. This capacity recovered in FY2017 to a level in FY2015, but its ROA (based on the core net business income) remains at a low approximately 0.1% level. JCR sees that enhancement of earnings capacity remains an issue facing the Bank.
- (2) Its core net business income for FY2017 was 2.4 billion yen, approximately twice as much as the income for FY2016. There was contribution from the increased gains on cancellation of investment trusts, but even excluding this effect, the core net business income significantly increased for FY2017 over FY2016. The increased net interest income and reduced expenses led the increase. Promoting improvement of efficiency including revisions to functions of branches largely reduced the expenses. The net interest income was increased by reduction of deposit interest and increase of interest and dividend on securities. These factors will continue supporting the core net business income for FY2018. With the decline of interest on loans and discounts which was not small, on the other hand, there remains an issue to address. The Bank sharply increased loans to SMEs with relatively high yield in FY2017. JCR will closely watch whether the Bank can reduce pace of the decline of interest on loans and discounts through sustaining the growth.
- (3) For the surplus fund management, it increased balance of securities such as investment trusts with relatively high yield and corporate bonds, while reducing due from banks, and the increase is contributing to the growth of income. The unrealized gains on bonds are working as buffer, but the interest rate risk amount for the surplus fund management is large against the core capital. The price fluctuation risk from the equity assets is also increasing. Given these factors, JCR will closely watch risk amount trend and conditions of risk management.
- (4) The Bank's non-performing loans ratio disclosed under the Financial Reconstruction Act, which is low as compared with the average of shinkin banks, has been sustainably falling. There are debtors classified as other debtors requiring caution and below this category who have large debts which are not covered by loan loss reserve, collateral, guarantees or other means, but its credit costs will remain stable for the time being, as it makes conservative loan loss provisions for large borrowers, of the uncovered debts exceed a certain level.
- (5) Its consolidated core capital ratio adjusted for allowance for loans losses, etc. stood high at more than 14% as of March 31, 2018. There is a possibility that the core capital ratio will continue declining due to an increase of risk assets as a result of growth of loans balance, but JCR sees that the Bank will retain its competitive advantage in the capital adequacy.

Kengo Sakaguchi, Tsuyoshi Ohishi

Rating

Issuer: Seto Shinkin Bank

<Affirmation>

Long-term Issuer Rating: A- Outlook: Stable



Rating Assignment Date: July 6, 2018

The criteria used for identifying matters which serve as assumptions for the assessment of the credit status, and the criteria used for setting of grades indicating the results of the assessments of the credit status are published as "Types of Credit Ratings and Definitions of Rating Symbols" (January 6, 2014) in Information about JCR Ratings on JCR's website (<https://www.jcr.co.jp/en/>).

Outline of methodology for determination of the credit rating is shown as "JCR's Rating Methodology" (November 7, 2014) and "Banks" (May 8, 2014) in Information about JCR Ratings on JCR's website (<https://www.jcr.co.jp/en/>).

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