

THANACHART SECURITIES PLC

No. 41/2018
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CORPORATES

Company Rating: A+
Outlook: Stable

Company Rating History:

Date	Rating	Outlook/Alert
28/04/15	A+	Stable
03/04/12	A	Stable

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RATIONALE

TRIS Rating affirms the company rating of Thanachart Securities PLC (TNS) at "A+". TNS's rating is enhanced from its stand-alone credit profile to reflect its status as a highly strategic subsidiary of the Thanachart Group. The stand-alone rating is based on TNS's experienced and prudent management team, its ability to maintain profitability in a highly competitive industry, and its sufficient liquidity and solid capital base. The rating also takes into account the potential that TNS will realize more benefits from the greater utilization of Thanachart Bank PLC's (TBANK) nationwide branch network and relationships with corporate clients.

The rating is, however, constrained by the cyclical and volatile nature of the securities industry and the downward pressure on commission rates from intensifying competition.

KEY RATING CONSIDERATIONS

A highly strategically important subsidiary of Thanachart Group

As a wholly-owned subsidiary of TBANK and a highly strategically important member of the Thanachart Group, TNS receives both business and financial support from its parent bank. TNS has been leveraging TBANK's branch network as a means to expand its base of retail clients. Cross-selling has been actively encouraged. For example, in 2017, 17% of TNS's new brokerage accounts were acquired through referrals from TBANK. Brokerage fees from accounts referred by TBANK made up 11% of the revenue TNS reported from securities brokerage fees in 2017.

TNS is also able to leverage TBANK's wide range of financial services to provide a full spectrum of solutions for its clients. In addition, TNS earns investment banking revenues and brokerage fees from providing services to related companies in the Thanachart Group.

In addition to business support, TNS receives financial support from TBANK. For example, TNS has been granted a large credit line by TBANK. Because of the business and financial support it receives from TBANK, TNS has an advantage over other securities firms that are not affiliated with a full-service commercial bank.

Profits and operating costs hold steady despite loss of market share

TNS's market share in the securities brokerage industry has fluctuated around 4% since 2010. However, competition has grown more intense. New firms entered the industry. There has been continuing downward pressure on the commission rates across the industry. TNS's market share dropped from 4.17% (ranked seventh in the industry) in 2016 to 3.78% (ninth) in 2017 and 3.32% (12th) for the first two months of 2018. Despite TNS's steady drop in market share, the revenue share in securities segment remained stable at 5.5% in 2016 (ranked fourth) and 5.1% (fourth) in the first six months of 2017.

TNS's average commission rate declined from 16 basis points (bps) in 2016 to 14 bps in 2017. Despite the drop, the rate was still higher than the industry average of 11 bps in 2017.

TNS's profitability has held steady, in line with the industry. Net profit was Bt609 million in 2017, a slight decline from Bt662 million in 2016 due to a decrease in brokerage fees from the securities segment. Fees and services

income increased from Bt135 million in 2016 to Bt160 million in 2017, which partially offset a decrease in revenues from the brokerage segment. The return on average assets (ROAA) on a non-annualized basis was 2.58% in the first six months of 2017. The ROAA was higher than the industry average of 1.63% during the same period despite TNS reported a drop in total revenue. The ratio was 6.3% in 2017. In addition, TNS's operating costs are less than industry peers. The ratio of operating expenses to net revenues was 55.8% for the first six months of 2017, compared with the industry average of 64.5% during the same period. The ratio was 52.2% in 2017.

Reliance on brokerage fees

Most of TNS's revenue comes from brokerage fees. This source is volatile and is under increasing pressure from the liberalization of brokerage fees. Brokerage fees constituted 68% of total revenue in the first six months of 2017, compared with the industry average of 61%. The proportion of brokerage fees to total revenue decreased from 74% in 2016 to 66% in 2017, while fees and services income increased from 6% in 2016 to 8% in 2017. Increases in underwriting fees and fees from selling agents drove the increase. Gains on trading increased from 3% of total revenue in 2016 to 6% in 2017. A more diverse revenue base should help stabilize TNS's earnings, amid more intense competition following the full liberalization of brokerage fees.

Exposure to market risk and credit risk

TNS's proprietary trading activities are limited to the pursuit of arbitrage investment opportunities and to hedge its positions in financial products sold. This strategy exposes the company to a lower level of market risk than firms that engage in speculative day trading operations. However, TNS continues to hold on its books two sizable investments in two listed companies. As of December 2017, these investments were worth Bt1.8 billion or 49% of total investments. TNS has no plan to liquidate these investments in the near future. TNS acquired these investments at low costs, and the investments yield solid dividend income. However, TNS carries a certain level of market risk, considering the size of the investments and the fact that TNS's investments are concentrated in just two securities.

TNS's credit risk exposure is considered sizable. The value of the margin loan portfolio increased from Bt3.5 billion in 2016 to Bt4.1 billion in 2017, representing 5.9% of industry-wide margin lending and 1.1 times TNS's equity. Nonetheless, TRIS Rating expects TNS will continue to control the credit risk of the margin loans by strictly enforcing margin calls and forced sales, and by maintaining its stringent criteria on collateral.

Sufficient liquidity and solid capitalization

As of December 2017, the ratio of liquid assets (cash and investments) to total assets was around 33%, compared with 23% at the end of 2015 due to higher trading securities from block trade products. Borrowings from financial institutions increased from Bt1.59 billion in 2015 to Bt2.99 billion in 2016 and Bt3.42 billion in 2017. TNS has available credit facilities from several financial institutions. The lines of credit should be enough to cover any temporary liquidity shortfall at the current scale of operations. TBANK provides approximately 75% of the total amount of available credit.

As of December 2017, shareholders' equity stood at Bt3.7 billion. This large capital base serves as a cushion against the credit risk of the margin loan portfolio and the market risk of TNS's large investments. The ratio of equity to adjusted assets, a measure of financial leverage, has been on a downward trend. The ratio declined from 71.1% in 2013, to 48.1% in 2016, and to 44.3% in 2017. The company ended 2017 with a net capital ratio (NCR) of 44%, compared with the regulatory requirement of 7%.

RATING OUTLOOK

The "stable" outlook reflects the expectation that TNS will maintain its status as a highly strategic subsidiary of the Thanachart Group and continue to receive strong support from TBANK.

RATING SENSITIVITIES

The rating and/or outlook of TNS could be revised downward should there be any changes in TBANK's credit profile or if our view changes on the degree of support TNS receives from TBANK. In contrast, the credit upside for TNS is limited, based on the current credit profile of TBANK.

COMPANY OVERVIEW

TNS entered the securities industry in 1980 under the name National Finance and Securities Co., Ltd. In 1997, the securities brokerage, proprietary trading, and underwriting operations, together with the related assets and receivables, were transferred to a newly established company, National Securities Co., Ltd. The transfer was in accordance with the government's policy for finance and securities companies to separate their businesses into a finance company and a

securities company. The company was converted into a public company in 2004, and later became Thanachart Securities PLC in 2005.

Prior to 2007, before The Bank of Nova Scotia Asia Ltd. became a strategic partner of TBANK, TNS was fully owned by Thanachart Capital PLC (TCAP), formerly known as National Finance PLC. As a part of TCAP’s reorganization plan, in July 2007, TBANK bought TNS from TCAP, along with seven other subsidiaries. TNS has been a wholly-owned subsidiary of TBANK since.

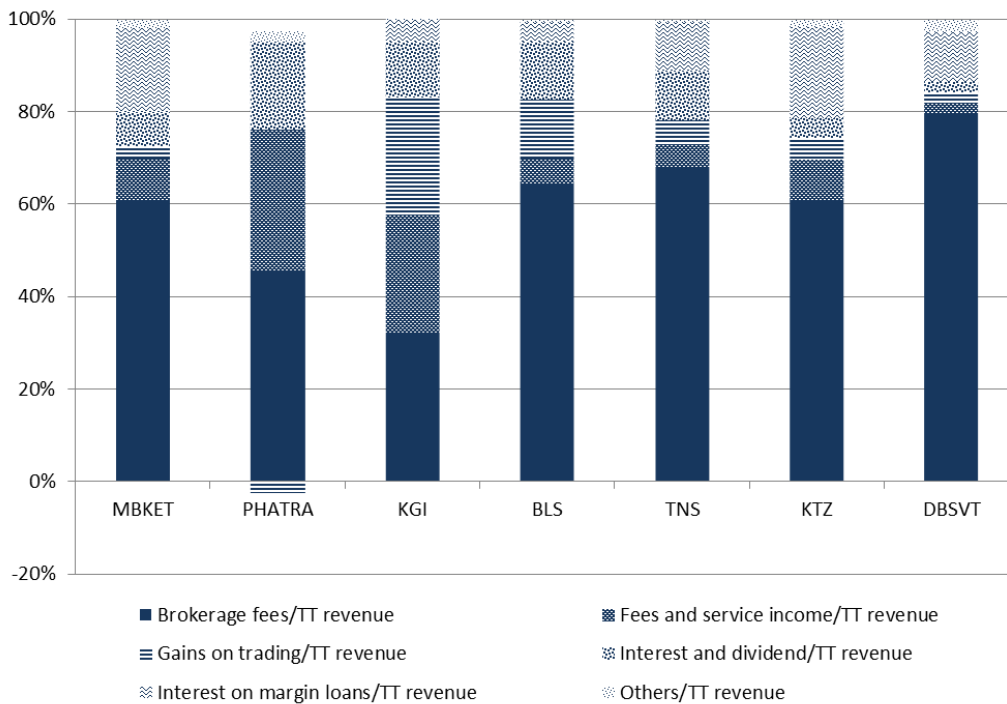
In 2010, TBANK acquired a 99.95% ownership stake in Siam City Bank PLC (SCIB). At the end of that year, TNS acquired the operations of Siam City Securities Co., Ltd. (SCIBS), which was a wholly-owned subsidiary of SCIB. Around 100 staff from SCIBS transferred to TNS. As of December 2016, TNS employed 531 staff and had a total of 34 branches in Bangkok and upcountry.

As a wholly-owned subsidiary of TBANK, TNS enjoys the use and the recognition of the “Thanachart” brand. TNS shares some network infrastructure with TBANK. It also outsources information technology services and the human resource function to TBANK.

TNS was granted a license to provide a full range of services in the securities business, including securities brokerage, securities trading, financial advisory and underwriting, investment advisory, derivatives brokerage, securities borrowing and lending (SBL), and acting as a selling agent for unit trusts. The company positions itself as a full-service premium broker, offering high-quality research, investment banking, offshore brokerage, and SBL services.

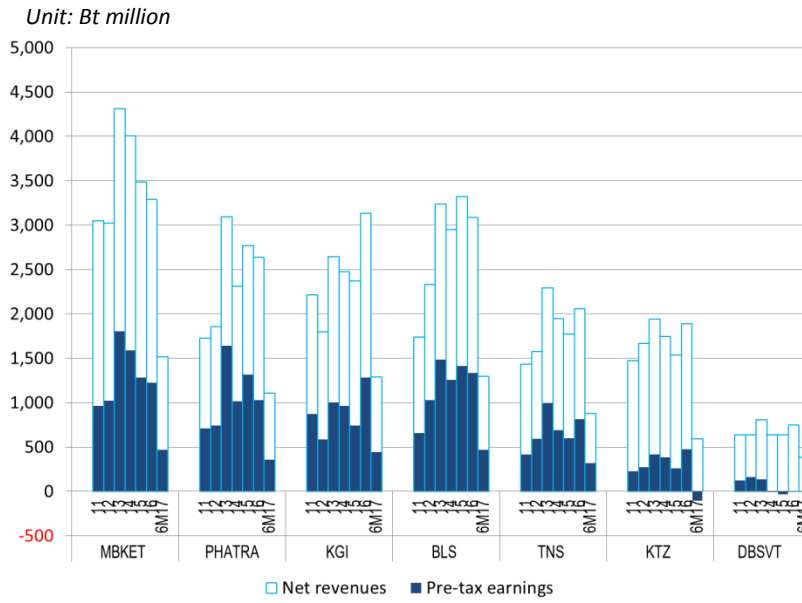
KEY OPERATING PERFORMANCE

Chart 1: Revenue Structure in 1H2017 (Jan-Jun 2017)



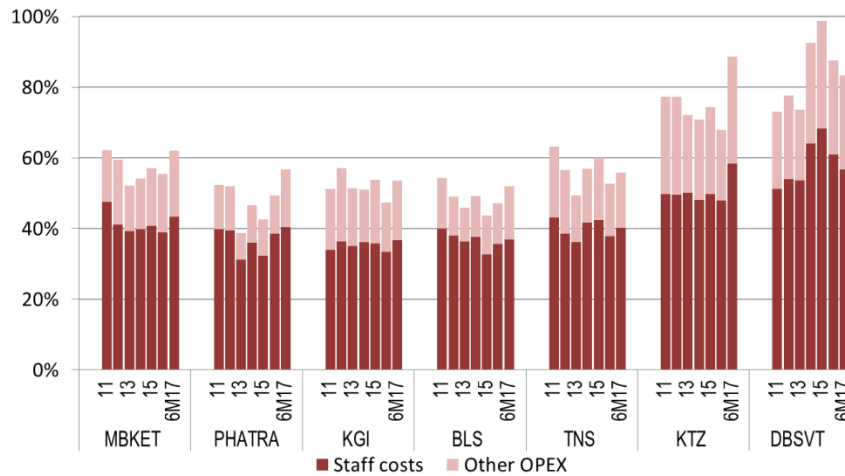
Source: Financial statements of each company

Chart 2: Net Revenues and Pre-tax Earnings of Selected Brokers in 2011-1H2017



Source: Financial statements of each company

Chart 3: Staff Cost and Other Operating Expenses of Selected Brokers in 2011-1H2017 (% of Net Revenues)



Source: Financial statements of each company

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS
Unit: Bt million

	-----Year Ended 31 December -----				
	2017	2016	2015	2014	2013
Total assets	11,764	9,479	7,438	7,587	6,587
Net Investment in securities	3,755	3,029	1,504	1,629	1,340
Total securities business receivables and accrued interest receivables	7,242	4,662	4,464	5,673	4,963
Allowance for doubtful accounts	14	14	113	171	172
Total debts	3,812	3,049	1,599	1,649	750
Shareholders' equity	3,675	3,380	3,145	3,257	3,393
Net securities business income	1,725	1,895	1,632	1,792	2,115
Total income	2,004	2,157	1,886	2,047	2,403
Operating expenses	981	1,085	1,061	1,106	1,130
Interest expenses	126	97	117	99	113
Net income	609	662	488	561	801

Unit: %

	-----Year Ended 31 December -----				
	2017	2016	2015	2014	2013
Profitability					
Brokerage fees/total revenues	66.0	74.2	76.3	76.9	76.0
Fees and services income/total revenues	8.0	6.3	1.7	5.4	6.3
Gain (loss) from trading/total revenues	5.7	2.6	1.5	0.9	2.2
Operating expenses/net revenues	52.2	52.7	60.0	56.8	49.3
Pre-tax margin	40.0	39.7	34.0	35.6	43.4
Return on average assets	6.3	7.8	6.5	7.9	11.8
Return on average equity	17.6	20.3	15.2	16.9	25.8
Asset Quality					
Classified receivables/gross securities business receivables	0.2	0.3	2.5	3.0	3.5
Allowance for doubtful accounts/gross securities business receivables	0.2	0.3	2.5	3.0	3.5
Credit costs (reversal)	0.0	0.0	(0.5)	0.0	0.0
Capitalization					
Equity/Adjusted assets	44.3	48.1	59.0	56.8	71.1
Liquidity					
Liquid assets/total assets	33.2	33.9	23.1	23.7	21.0
Liquid assets/adjusted assets	47.0	45.8	32.2	31.4	29.0
Less liquid assets/long-term capital	112.8	108.2	110.3	115.1	95.8

Thanachart Securities PLC (TNS)

Company Rating:

A+

Rating Outlook:

Stable

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