

# BANK OF AYUDHYA PLC

No. 197/2019  
29 November 2019

## FINANCIAL INSTITUTIONS

**Company Rating:** AAA  
**Outlook:** Stable

**Last Review Date:** 06/12/18

### Company Rating History:

Date	Rating	Outlook/Alert
23/12/13	AAA	Stable
08/07/13	AA-	Positive
17/04/09	AA-	Stable
04/04/08	A+	Positive
23/11/04	A	Stable
12/07/04	A-	Positive
07/10/03	A-	-

### Contacts:

Annop Supachayanont, CFA  
annop@trisrating.com

Sithakarn Tongphiphat, FRM  
sithakarn@trisrating.com

Jittrapan Pantaleard  
jittrapan@trisrating.com

Narumol Charnchanavivat  
narumol@trisrating.com



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## RATIONALE

TRIS Rating affirms the company rating on Bank of Ayudhya PLC (BAY) at “AAA”. The rating outlook remains “stable”. The rating reflects BAY’s status as a highly strategic member of Mitsubishi UFJ Financial Group (MUFG Group), the largest financial group in Japan. The rating also reflects the business and financial support the MUFG Group has provided to the bank and the expected support from its parent group in times of financial distress. BAY is a subsidiary of MUFG Bank Ltd. (MUFG Bank). MUFG Bank is a wholly-owned subsidiary and a core member of the MUFG Group (rated “A/Positive” by S&P Global Ratings).

BAY’s stand-alone credit profile reflects its well-diversified business mix and franchise strengths in the retail and Japanese corporate banking segments. However, BAY’s moderately strong capital and somewhat above-average reliance on wholesale funding relative to large Thai banks constrain its standalone-credit profile.

## KEY RATING CONSIDERATIONS

### A highly strategic subsidiary of the MUFG Group

TRIS Rating expects BAY to receive extraordinary support from the MUFG Group in times of financial distress. We also expect the Group to continue to provide business and funding support to BAY, despite the bank’s modest revenue and earnings contributions.

We believe the MUFG Group has a strong and long-term commitment to support BAY given its 76.88% ownership. We think there is a linkage between BAY and the Group’s reputation due to BAY’s closer collaboration with the MUFG Group to support both of their clients. Key areas of collaboration include facilitating cross-border businesses, client referral, supply-chain financing, and wealth management. We also factor in the active involvement of the MUFG Group at the board and management levels.

### Solid and expanding franchise

BAY’s rating is underpinned by its solid banking franchise. The bank was designated as one of Thailand’s five Domestic Systematically Important Banks (D-SIBs) in 2017. Since then it has continued to expand its loan market share among 11 listed Thai commercial banks, archiving a 14.5% share as of the third quarter of 2019 (Q3/19). The ability to sustain stronger loan growth than its peers in all segments over recent years has helped the bank enlarge its market share. BAY’s loan book expanded by 7.8% year-on-year (y-o-y) in 2018, with small and medium enterprise (SME) and retail lending being the key drivers. As of Q3/19, year-to-date (y-t-d) growth was 6.4%, driven by growth in all major segments.

### Retail banking drives earnings

We expect retail banking to remain a primary earnings driver of BAY over the next three years. Retail businesses contributed around 70% of BAY’s net income in 2018. BAY is a major auto hire-purchase (HP) lender with market shares, according to our database, reaching a significant 20% across HP providers in Thailand at the end of 2018. The bank is also a key mortgage lender with a market share of 11% across Thai commercial banks.

To mitigate the potential impacts from financial technology (fintech) disruption, BAY has invested in new technology in a pre-emptive move, aiming

to deliver banking and financial services through digital channels and improved efficiency. This should help the bank retain its large retail customer base and sustain its competitiveness as technological disruption intensifies.

### **Diversifying revenue structure**

BAY's revenue structure is relatively diversified. Net fee income made up around 19% of total revenue during 2018 and Q3/19 (adjusted for proceeds from sale of Ngern Tid Lor Co., Ltd. (NTL)), close to the average for Thai commercial banks. Consumer finance businesses generate the majority of fee income, with around 80% of total fees coming from credit card, bancassurance, and transaction- and loan-related fees. Other key non-net interest income (non-NII) includes gains on foreign exchange (FX) and bad debt recoveries.

Collaboration with the MUFG Group should further help diversify BAY's earnings by enhancing BAY's capacity to offer cross-border financial services in areas of investment banking, transaction banking, and wealth management. Similarly, continued regional expansion, which complements the MUFG Group's regional strategy, should gradually help diversify the bank's earnings.

### **Well-managed asset quality**

We expect BAY to be able to keep its overall asset quality under control and maintain healthy provisions. Soft economic headwinds continue to pressure the asset quality of Thai commercial banks as the industry average non-performing loan (NPL) ratio<sup>1</sup> remains at an elevated 3.17% level as of Q3/19. However, BAY has been able to maintain good asset quality, with a relatively low NPL ratio at 1.95% as of Q3/19. BAY's NPL formation, inclusive of bad-debt write offs, has also remained relatively stable at an annualised 1.2% during the first nine months of 2019. We attribute this to the bank's strong risk management. Apart from prudent underwriting standards, the bank uses a sector-based approach to monitor the loan quality of borrowers along the supply chain of its focused sectors to mitigate the deterioration of asset quality. The focused sectors include the auto and property industries. Active write-offs of delinquent loans also help BAY maintain a relatively low NPL ratio.

In terms of loan loss reserve, BAY has maintained a relatively conservative provisioning policy. The bank continues to build up its provision, as reflected by credit costs at the 1.5%-1.6% level during 2018 and Q3/19. The resulting NPL coverage ratio as of Q3/19 stood at 162%, slightly above the average for Thai commercial banks.

### **Average profitability**

We expect BAY's profitability level to remain on par with the average for Thai commercial banks over the next few years. Healthy risk-adjusted returns and high operating expenses should continue to be among the major factors behind BAY's moderate profitability. Although its strength in the retail business and well-controlled asset quality should help the bank sustain high risk-adjusted loan yields, high operating expenses from its retail businesses and on-going IT spending may put pressure on the bank's profitability. We forecast a risk-adjusted net interest margin (NIM) in the 2.3%-2.4% range over the next three years. The figure was 2.3%-2.4% during 2018 and Q3/19, above that of several major Thai banks. We forecast a cost-to-income ratio close to an elevated 50% level over the same period.

### **Sufficient capital to support growth**

As a D-SIB bank, BAY is required to maintain an additional 1% of core equity tier-1 (CET-1) on top of the 8% minimum requirement by 2020. We estimate BAY's CET-1 ratio should remain well above the requirement, close to its current level at around 12%-13% over the next three years. Our estimate of CET-1 is based on the assumption of 7% loan growth and a 25% dividend pay-out ratio over the next three years. Compared with other Thai banks, whose average was 15.9% for Q3/19, BAY's capital ratio is considered moderately strong.

### **Average funding**

We consider BAY's funding profile to be fairly strong and diversified for a Thai commercial bank. BAY's deposit franchise is relatively large, with a 12.2% market share in deposits across Thai commercial banks as of Q3/19. BAY places more reliance on wholesale funding and carries higher-cost term deposits, compared with the major Thai banks. As of Q3/19, deposits made up 79% of BAY's total funding, below the Thai commercial bank average of 87%. Current account-savings account (CASA) stood at 42% of total deposits as of Q3/19, below the Thai commercial bank average of around 60%. Funding cost stood at an annualised 1.8% during the first nine months of 2019, above that of other large Thai banks.

We have no concerns over the bank's reliance on wholesale funding as we view that it is appropriate for its asset profile, with fixed-rate HP lending representing a large proportion of 23% of its portfolio as of Q3/19. Moreover, parent funding helps enhance its deposit franchise, since we view borrowing from the MUFG Group to be a stable wholesale funding source.

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<sup>1</sup> Including interbank

BAY continues to expand its deposit base to be in line with loan growth. In Q3/19, total deposits have expanded 4.8% y-t-d, driven mainly by growth in term deposits. Going forward, a broadened client base, notably among SMEs, should allow BAY to raise more CASA funding.

### Adequate liquidity

We consider BAY has adequate liquidity on a stand-alone basis; its liquidity profile is on par with other mid-sized Thai banks. The bank's liquidity coverage ratio (LCR) is below the Thai commercial bank average of 180% but remains fairly healthy at 136% at the end of H1/19 and well above the regulatory requirement of 90%. For Q3/19, BAY's liquid assets to total deposits were at a satisfactory 28% level. We view available credit facilities and the support the bank receives from the MUFG Group to be strong back-up for its liquidity.

### BASE-CASE ASSUMPTIONS

The followings are our base-case assumptions for BAY's performance during 2019-2021:

- Loan growth: around 7%
- Credit cost: around 1.4%-1.5%
- NPL ratio: around 2.0%
- CET-1 ratio: 12%-13%
- Risk-adjusted NIM: around 2.3%-2.4%

### RATING OUTLOOK

The "stable" rating outlook reflects the expectation of TRIS Rating that BAY will remain a highly strategic subsidiary of the MUFG Group and continue to receive strong support from its parent bank.

### RATING SENSITIVITIES

The credit rating and/or outlook of BAY could change if the credit profile of the MUFG Group changes or if TRIS Rating's view of the strategic importance of BAY to the Group changes.

### COMPANY OVERVIEW

BAY was established in 1945 and listed on the Stock Exchange of Thailand (SET) in 1977. Following the 1997 Asian financial crisis, BAY set up the Asset Quality Improvement Department in 1999. It established Krungsri Ayudhya AMC Ltd. (KAMC; formerly Ayudhya Asset Management Co., Ltd.) in 2000 to resolve its troubled loans. In 2001, BAY joined with GE Capital Thailand Co., Ltd. (GECT) to enter the credit card business by setting up Krungsri Ayudhya Card Co., Ltd. (KCC). BAY also invested in a fund management company, Krungsri Asset Management Co., Ltd. (KSAM; formerly Ayudhya Fund Management Co., Ltd. and AJF Asset Management Ltd.). In 2005, BAY increased its stake in Ayudhya Development Leasing Co., Ltd. (ADLC) and raised its ownership stake in Krungsri Factoring Co., Ltd. (KSF; formerly Ayudhya Factoring Co., Ltd.). In the same year, BAY purchased 86% of the shares of Krungsri Securities PLC (KSS; formerly Ayudhya Securities PLC). In 2006, to seize opportunities in the HP lending segment, BAY established two wholly-owned subsidiaries. Ayudhya Capital Lease Co., Ltd. (AYCL) was created to offer new car financing and inventory finance, while Ayudhya Auto Lease PLC (AYAL) was established to make hire-purchase auto loans.

In 2007, GE Capital International Holding Corporation (GECIH) became the new major shareholder of BAY, taking a 34.9% stake. GECIH's stake was diluted to 32.9% in 2008 after warrant-holders exercised the last lot of warrants. In 2008, BAY established a new subsidiary, Ayudhya Hire Purchase Co., Ltd. (AYHP), to make HP loans on a sale and leaseback basis. In addition, BAY acquired all the ordinary shares of Ayudhya Capital Auto Lease PLC (AYCAL; formerly GE Capital Auto Lease PLC) from General Electric Capital Asia Investment, Inc. (GECAL) and other shareholders. On the transfer date, AYCAL had outstanding loans of Bt75.3 billion. After acquiring AYCAL, BAY restructured its auto HP subsidiaries into a single subsidiary to offer one-stop total solutions. AYCAL merged all the auto HP activities from its three subsidiaries: AYCL, AYAL, and AYHP. In 2009, BAY completed the acquisitions of AIG Retail Bank PLC (AIGRB) and AIG Card (Thailand) Co., Ltd. (AIGCC), for a combined price of Bt1.6 billion. In November 2009, BAY acquired GE Money Thailand (GEMT), which had a retail loan portfolio of Bt45.8 billion. In the first quarter of 2012, BAY successfully acquired and integrated the Thai retail banking business of Hongkong and Shanghai Banking Corporation Ltd. (HSBC). HSBC had a loan portfolio of Bt13.9 billion and deposits of Bt9.6 billion.

In September 2012, GECIH reduced its stake in BAY to 25.33% by selling the shares it held in block trades. In July 2013, GECIH and MUFG Bank signed a Share Tender Agreement regarding GECIH's shareholding in BAY. The agreement called for MUFG Bank to make a voluntary tender offer for all of BAY's shares at Bt39 per share. GECIH participated in the offer and tender for its entire shareholding. The tender offer was completed in December 2013. MUFG Bank became BAY's strategic

shareholder, holding a 72.01% stake.

In accordance with the one-presence policy of the Bank of Thailand (BOT), MUFG Bank, Bangkok branch was integrated with BAY in January 2015. BAY issued new common shares to MUFG Bank in exchange for the assets, liabilities, and all the commercial operations of MUFG Bank, Bangkok. As a result, MUFG Bank's shareholding in BAY increased to 76.88% from 72.01%. The founding family, the Ratanarak Group, remains a key partner, as it owns approximately 20% of BAY's shares.

In September 2016, BAY completed a 100% acquisition of Hattha Kaksekar Ltd. (HKL), a micro-finance institution in Cambodia, with a 100% shareholding. The newly acquired business contributed an additional Bt14.30 billion of loans, representing 1% of BAY's total loan portfolio, and Bt11.78 billion of deposits, representing 1.1% of BAY's total deposits, based on its consolidated financial statements.

On 28 February 2019, BAY sold 50% of its interest in its subsidiary, NTL. In H1/19, BAY recognised gains on the sale of investments in subsidiaries of Bt8.63 billion, based on its consolidated financial statements.

On 8 August 2019, BAY entered into a Share Purchase Agreement whereby it agreed to buy 50% of the total issued and paid-up share capital of SB Finance Company Inc. (SBF) of the Philippines from Security Bank Corporation (SBC). As of H1/19, contributions from foreign businesses accounted for 2% of loans and 3.8% of pre-tax profits on a consolidated basis. BAY has a presence in Cambodia, Lao People's Democratic Republic (Lao PDR), and Myanmar, through branches, subsidiary companies or representative offices.

## FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS<sup>1</sup>

Unit: Bt million

	Jan-Sep 2019 <sup>2</sup>	----- Year Ended 31 December -----			
		2018	2017	2016	2015
Total assets	2,269,189	2,173,622	2,088,771	1,883,188	1,705,516
Average Assets	2,221,406	2,131,197	1,985,980	1,794,352	1,458,439
Investment in securities	127,314	137,369	86,156	133,701	111,603
Loans and receivables	1,783,350	1,676,344	1,554,321	1,452,746	1,307,027
Allowance for doubtful accounts	66,488	61,360	55,476	49,462	44,944
Deposits	1,495,047	1,426,348	1,319,229	1,108,288	1,046,290
Borrowings <sup>3</sup>	407,385	399,747	422,587	474,726	383,180
Shareholders' Equities	263,670	243,718	225,987	208,768	190,748
Average Equities	253,694	234,853	217,378	199,758	161,209
Net interest income	57,295	75,329	68,535	61,977	56,351
Non-interest income <sup>4</sup>	35,707	34,251	31,946	29,510	26,423
Total revenue	93,002	109,580	100,481	91,487	82,774
Operating expenses <sup>5</sup>	39,662	51,741	48,210	43,080	38,947
Pre-provision operating profit (PPOP)	53,340	57,839	52,271	48,407	43,826
Impairment losses on loans and securities	20,016	26,180	22,970	21,315	20,186
Net income	26,602	25,192	23,561	21,684	18,853
Net fee and service income	15,981	21,248	19,675	18,175	17,229
Gains on investments	9,188	374	896	599	409

1 Consolidated financial statements

2 Non-annualised and unaudited

3 Including interbank and money market

4 Net of fees and service expense

5 Excluding fees and service expense

Unit: %

	Jan-Sep 2019 <sup>2</sup>	----- Year Ended 31 December -----			
		2018	2017	2016	2015
<b>Earnings</b>					
Return on average assets <sup>6</sup>	1.63	1.18	1.19	1.21	1.29
Interest spread <sup>6</sup>	3.30	3.44	3.37	3.36	3.71
Net interest margins <sup>6</sup>	3.54	3.67	3.58	3.57	3.98
Net interest income/average assets <sup>6</sup>	3.44	3.53	3.45	3.45	3.86
Non-interest income <sup>7</sup> /average assets <sup>6</sup>	2.14	1.61	1.61	1.64	1.81
Net fee and service income/total revenue	17.18	19.39	19.58	19.87	20.82
Cost-to-income	42.65	47.22	47.98	47.09	47.05
<b>Capitalisation</b>					
CET-1 ratio <sup>8</sup>	13.03	12.46	12.56	12.14	12.22
Tier-1 ratio <sup>8</sup>	13.23	12.52	12.64	12.24	12.33
BIS ratio <sup>8</sup>	17.81	16.15	16.50	15.06	14.50
CET-1/BIS ratio <sup>8</sup>	73.15	77.17	76.12	80.61	84.28
<b>Asset Quality</b>					
Credit costs <sup>6</sup>	1.55	1.62	1.53	1.54	1.74
Non-performing loans/total loans <sup>9</sup>	1.95	2.00	2.00	2.11	2.15
Allowance for loan losses/non-performing loans	161.94	155.52	143.99	138.58	134.06
<b>Funding &amp; Liquidity</b>					
CASA/total deposit	42.32	43.93	44.55	52.69	51.52
Loan/total deposits	118.96	117.22	117.52	130.73	124.58
Deposits/total liabilities	74.55	73.91	70.82	66.19	69.07
Liquid assets/total deposits <sup>10</sup>	24.24	24.84	28.33	25.88	25.57
Liquid assets/short-term liabilities <sup>11</sup>	n.a.	25.90	28.13	25.01	24.80

6 Annualised

7 Net of fee and service expenses

8 Consolidated basis

9 Including interbank; excluding accrued interests

10 Including interbank borrowing

11 Financial liabilities with maturity less than one year

**RELATED CRITERIA**

- Commercial Banks, 30 March 2017
- Group Rating Methodology, 10 July 2015

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**Bank of Ayudhya PLC (BAY)**

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<b>Company Rating:</b>	AAA
<b>Rating Outlook:</b>	Stable

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**TRIS Rating Co., Ltd.**

Silom Complex Building, 24th Floor, 191 Silom Road, Bangkok 10500, Thailand Tel: 0-2098-3000

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