KIATNAKIN PHATRA BANK PLC

No. 56/2022
8 April 2022

FINANCIAL INSTITUTIONS

Company Rating:	A
Issue Ratings:	
Senior unsecured	A
Basel III Tier 2 Subordinated	BBB+
Outlook:	Stable

Last Review Date: 23/04/21

Company Rating History:

Date	Rating	Outlook/Alert
26/04/19	A	Stable
25/04/18	A-	Positive
31/03/15	A-	Stable
31/03/11	A-	Positive
30/11/04	A-	Stable
12/07/04	BBB+	Positive
21/05/02	BBB+	-
21/06/00	BBB	-
06/03/00	BBB	Alert Negative
25/11/99	BBB	-

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RATIONALE

TRIS Rating affirms the company rating on Kiatnakin Phatra Bank PLC (KKP) at "A" and the ratings on KKP's Basel III Tier 2 subordinated debt at "BBB+" with a "stable" outlook. At the same time, TRIS Rating assigns the rating of "A" to KKP's proposed issue of up to THB10 billion in senior unsecured debentures due within three years under the Medium-Term Notes Program (MTN). The ratings take into account KKP's well-diversified sources of revenue, adequate capital supported by solid profitability, and manageable asset quality.

KEY RATING CONSIDERATIONS

Strengthening commercial banking franchise

Our assessment of KKP's business position reflects its strengthening commercial banking franchise and strong market position in investment banking and private banking businesses. We believe KKP's commercial banking franchise will strengthen further, underpinned by an increase in business collaborations between its commercial banking operations and its strong capital market businesses. Key collaborations include provisions of banking and capital market solutions, an offering of deposit accounts at KKP to wealth clients of its securities subsidiary (Kiatnakin Phatra Securities) for settlement of investment transactions, and customer referrals within the group.

We anticipate KKP will be able to steadily expand its retail lending operation during the next few years, driven mainly by auto loans and home loans. In 2021, KKP's auto loans and home loans grew significantly by 22.3% and 40.5% respectively. Growth in the auto lending was mainly backed by its focus on top-selling brands and new customers with acceptable credit profile. The bank's enlarged retail lending operation is a positive development as it provides a good opportunity for cross-selling in the future.

Well-diversified earnings mix supports earnings growth

In our view, KKP has demonstrated resilient performance amid the Coronavirus Disease 2019 (COVID-19) pandemic, compared with its peers. KKP's earnings in 2021 has already surpassed its pre-COVID-19 level in 2019 whereas those of most Thai commercial banks remained below their pre-COVID-19 levels. This was mainly attributed to its diversified sources of earnings and well-controlled operating costs. KKP's commercial banking business accounted for 60% of the bank's consolidated earnings in 2021, followed by capital market business (29%) and debt restructuring business (11%). This demonstrates the benefit of KKP's diversified sources of earnings, which has helped alleviate the impact from the economic downturn.

Adequate capital position

We assess KKP's capital position as adequate with a projected common equity tier-1 (CET-1) ratio in the range of 13.3%-13.5% in 2022-2024. Our projection takes into account our loan growth assumption of 10-12% per annum in 2022-2024, driven mainly by auto lending and home loans. We assume the bank's dividend payout ratio to be 40% in 2022-2024. The CET-1 ratio at the end of 2021 was 13.62%, slightly lower than 14.33% at the end of 2020. This was mainly due to the bank's strong portfolio expansion in 2021. At the same time, CET-1 made up 78.5% of total capital, indicating average quality of capital.

Strong earnings capacity maintained

KKP's earnings capacity remains its rating strength. The bank's return on average assets (ROAA) improved to 1.59% in 2021 from 1.52% in 2020, well above the industry average of 0.81% during the same period. The bank's strong profitability was attributed to higher net interest income, solid performance of capital market businesses, and well-controlled operating costs. We expect KKP's earnings capacity to remain strong over the next three years, with projected ROAA in the range of 1.34%-1.64% in 2022-2024. This is despite the declining net interest margin due to rising funding cost.

Asset quality deteriorated but manageable

KKP's risk position is still assessed as adequate on the back of its manageable asset quality. The bank's non-performing loans (NPL) ratio (excluding Purchased or Originated Credit Impaired (POCI) or distressed assets) at the end of 2021 was 3.1%, up marginally from 2.9% at the end of 2020. The increase was consistent with our expectation of a gradual deterioration in asset quality following the expiration of debt relief programs. Looking forward, KKP's NPL ratio (excluding POCI) may continue to rise further but is likely to remain under control.

At the end of 2021, KKP's loans under the debt relief program were around 11% of total loans, relatively stable compared with the end of 2020 and lower than the industry average of 14%. The majority of those remaining in the program are mainly in the auto hire purchase (HP) lending and commercial lending segments. Loans in the commercial lending segment are mostly secured by apartments or hotels, which despite having been hit hard by the COVID-19 pandemic, remain manageable due to the low loan-to-value of about 50%. KKP continues to offer long-term comprehensive debt restructuring to viable customers in this segment to support them during the gradual recovery of the tourism industry.

We are of the view that KKP has sufficient provisioning buffers against potential credit losses in the future. At the end of 2021, the bank's NPL coverage ratio was 175%, relatively stable and higher than the industry average of 162.6%. KKP's provisions for expected credit loss to average loans (credit cost) over the next few years are likely to fall gradually from 2021 but should be sufficient to absorb further deterioration in asset quality.

Improving funding profile due to better deposit mix

KKP has made good progress in improving its deposit franchise in recent years, and we expect this to continue. The bank's current account and savings account (CASA) deposits to total deposits rose to 59% at the end of 2021 from 53% at the end of 2020. This is the highest level among smaller banks. The improvement was mainly led by the offering of deposit accounts for the settlement of investment transactions to its wealth management clients (dubbed KKP Smart Settlement or KKPSS), corporates deposits, and e-saving accounts.

KKP can acquire deposits at lower cost without expanding physical branches. This is due to the collaborations between its commercial banking business and its capital market businesses. KKP's cost of deposit was 1.16% in 2021, down from 1.8% in 2020. Despite its deposit cost in 2021 remaining above the industry average of 0.73%, the gap gradually narrowed to 0.43% in 2021 from 1.14% in 2016. While we view the expansion of deposit base and the narrower gap in deposit cost positively, its funding profile is still constrained by deposit concentration given the nature of KKPSS depositors which are mostly its wealth management clients.

Adequate liquidity

We view KKP's liquidity position as adequate over the next 12 months. As of the end of 2021, liquid assets made up 31.4% of total deposits, sufficient and above our cautionary threshold of 20%. The bank's liquidity coverage ratio (LCR) was at an average of 115.3% at the end of second quarter of 2021, above the regulatory requirement albeit weaker than the average for Thai banks of 186.7% reported by the Bank of Thailand (BOT).

BASE-CASE ASSUMPTIONS

The following are our base-case assumptions for KKP during 2022-2024:

- Loan growth: 10%-12%
- Net interest margin: 3.62%-4.05%
- Cost-to-income: 39.5%-42.4%
- Credit cost: 1.45%-2.1%
- NPL ratio (excluding POCI and interbank assets): 3.35%-3.67%
- CET-1 ratio: 13.27%-13.52% (excluding planned asset revaluation)

RATING OUTLOOK

The "stable" outlook reflects our expectation that KKP will maintain its adequate capital, asset quality at acceptable levels, and further cultivate synergies with its capital market and wealth management units to sustain healthy financial performance and revenue structure diversification.

RATING SENSITIVITIES

The ratings and/or outlook could be revised upward if KKP strengthens its capital position significantly, with the CET-1 ratio above 15% for a sustained period, while continuing to improve its asset quality and commercial banking franchise. We could revise the ratings downward if capital, asset quality and/or earnings capacity weakens materially.

COMPANY OVERVIEW

KKP, formerly known as Kiatnakin Finance and Securities Co., Ltd., was established by the Wattanavekin family in 1971. KKP was listed on the Stock Exchange of Thailand (SET) in 1988 and became a public company in 1993. In August 1997, KKP was one of 57 financial institutions with operations suspended due to the Asian financial crisis. After submitting and receiving regulatory approval for a rehabilitation plan, KKP resumed operations in April 1998. In July 1999, KKP's finance and securities business was split into two separate companies: Kiatnakin Finance PLC, operating the finance business, and Kiatnakin Securities Co., Ltd., operating the securities business.

Following the financial crisis, KKP began a new business, distressed asset management, by purchasing portfolios of troubled loans from the Financial Sector Restructuring Authority and other financial institutions. In 2000, KKP started to expand by offering residential property development project loans to small and medium enterprise (SME) real estate developers.

In December 2004, the Ministry of Finance (MOF) granted KKP a commercial banking license. KKP commenced universal banking operations in October 2005, and later changed its name to "Kiatnakin Bank PLC". In order to expand the scope of its business to include fund management, KKP purchased 60% of the shares of Kiatnakin Phatra Asset Management Co., Ltd. (KKPAM, formerly named Siam City Asset Management Co., Ltd.) in July 2011, and acquired the remaining 40% stake in September 2012.

Table 1: KKP's Group Structure

Source: KKP's information (as of 8 April 2022)

As a part of its growth strategy, KKP merged with KKP Capital Co., Ltd. (KKP CAPITAL) in September 2012, and later created a new brand name for the Group: "Kiatnakin Phatra Financial Group" (KKP). KKP's shareholding structure changed after the merger. KKP and its subsidiaries reorganized their businesses based on three strategic focuses: (i) Credit Business, (ii) Private Banking, and (iii) Investment Banking.

To streamline its business operations, KKP later sold all its shares in KKTRADE, which operated securities business for retail clients to Yuanta Securities (Thailand) Co., Ltd. in July 2016.

As of April 2021, KKP held 99.9% shares on KKP CAPITAL, while KKP CAPITAL held shares of Kiatnakin Phatra Securities PLC (KKPS) and Kiatnakin Phatra Asset Management (KKPAM). KKP Tower, another subsidiary of KKP, operates the office rental and property management business for the bank and subsidiary companies.

In November 2021, KKP Capital established new subsidiary under the name "KKP Dime Company Limited". KKP Dime's main objectives are to provide financial and investment services through digital channels. Kiatnakin Phatra Financial Group through KKP Capital Public Company Limited holds 100% of the total shares of KKP Dime.

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS

Unit: Mil. THB

	Year Ended 31 December				
	2021	2020	2019	2018	2017
Total assets	436,123	363,411	311,690	306,329	259,335
Average assets	399,767	337,551	309,010	282,832	246,556
Interbank and money market items	55,238	32,771	11,982	28,200	11,511
Investments	39,205	34,603	39,201	29,781	34,048
Loans and receivables	315,653	271,951	238,267	229,066	193,087
Loan loss reserves	16,620	13,234	10,589	10,760	10,576
Deposits	288,382	251,526	172,174	181,694	132,878
Borrowings[2]	62,169	39,504	76,253	63,358	64,947
Shareholders' equities	51,162	46,626	44,011	42,341	41,548
Average equities	48,894	45,318	43,176	41,944	41,032
Net interest income	15,701	14,679	12,316	11,262	10,628
Net fees and service income	6,074	4,336	4,604	4,579	4,055
Non-interest income[3]	9,131	6,969	7,436	7,544	6,173
Total revenue	24,831	21,648	19,752	18,806	16,802
Operating expenses[4]	9,745	9,758	9,355	9,232	8,369
Pre-provision operating profit (PPOP)	15,087	11,890	10,397	9,574	8,432
Expected credit loss	7,290	5,404	3,099	2,186	1,476
Net income	6,355	5,143	5,990	6,044	5,766

1 *Consolidated financial statements*
2 *Including interbank and money market*
3 *Net of fee and service expenses*
4 *Excluding fee and service expenses*

Unit: %

	Year Ended 31 December				
	2021	2020	2019	2018	2017
Earnings					
Return on average assets	1.59	1.52	1.94	2.14	2.34
Net interest margins	4.28	4.73	4.28	4.27	4.63
Risk-adjusted net interest margins	2.29	2.99	3.20	3.44	3.98
Net interest income/average assets	3.93	4.35	3.99	3.98	4.31
Non-interest income[5]/average assets	2.28	2.06	2.41	2.67	2.50
Net fees and service income/total revenue	24.46	20.03	23.31	24.35	24.14
Cost-to-income	39.00	41.16	46.73	47.80	48.17
Capitalization					
CET-1 ratio[6]	13.62	14.33	13.61	13.56	14.61
Total capital ratio[6]	17.35	18.28	17.20	17.26	17.69
CET-1/Total capital[6]	78.48	78.38	79.12	78.53	82.59
Asset Quality					
Credit costs	2.55	2.15	1.33	1.04	0.80
Non-performing loans/total loans[7]	3.09	2.93	4.03	4.13	5.02
Loan loss reserves/non-performing loans[7]	174.98	170.74	110.77	114.42	109.60
Funding & Liquidity					
CASA/total deposit[8]	59.06	52.49	37.54	38.36	40.55
Loan/total deposits[8]	106.42	105.27	137.73	125.43	145.31
Deposits[8]/total liabilities	74.91	79.40	64.32	68.83	61.01
Liquidity coverage ratio	N.A.	141	119	115	103
Liquid assets/total assets	21.94	18.95	16.78	19.95	19.01
Liquid assets/total deposits[9]	31.37	26.30	27.59	31.36	34.92

5 Net of fee and service expenses
6 Bank-only
7 Based on reported NPL, excluding accrued interests and interbank assets
8 Excluding bills of exchange and interbank borrowing
9 Including bills of exchange and interbank borrowing

RELATED CRITERIA

- Bank Hybrid Capital Rating Methodology, 24 December 2021
- Issue Rating Criteria, 15 June 2021
- Banks Rating Methodology, 3 March 2020

Kiatnakin Phatra Bank PLC (KKP)

Company Rating:	A
Issue Ratings:	
KKP30NA: THB2,000 million Basel III Tier 2 capital securities due 2030	BBB+
KKP314A: THB2,852 million Basel III Tier 2 capital securities due 2031	BBB+
Up to THB10,000 million senior unsecured debentures due within 3 years under the Medium-Term Notes Program	A
Rating Outlook:	Stable

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