

PHATRA SECURITIES PLC

No. 51/2018
26 April 2018

FINANCIAL INSTITUTIONS

Company Rating: A-
Outlook: Positive

Company Rating History:

Date	Rating	Outlook/Alert
13/06/13	A-	Stable

Contacts:

Preeyaporn Kosakarn

preeyaporn@trisrating.com

Annop Supachayanont, CFA

annop@trisrating.com

Raithiwa Naruemol

raithiwa@trisrating.com



WWW.TRISRATING.COM

RATIONALE

TRIS Rating affirms the company rating of Phatra Securities PLC (PHATRA) at “A-”. The rating reflects PHATRA’s status as a core subsidiary of the ultimate parent company, Kiatnakin Bank PLC (KK, rated “A-/Positive” by TRIS Rating), with a strong profit contribution and close linkage to the Kiatnakin Phatra Financial Group (KKP). At the same time, TRIS Rating revises the rating outlook of PHATRA to “positive” from “stable”. The outlook revision follows the rating action on the parent bank, KK, as the ratings of the two entities are linked.

The company rating of PHATRA also reflects the company’s well-diversified revenue base, established brokerage franchise among institutional investors and high net worth clients, leading market position in investment banking, and strong financial performance. 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. The market risk associated with the company’s principal investment activities also affects the risk profile of the company.

KEY RATING CONSIDERATIONS

A core subsidiary of Kiatnakin Bank PLC (KK)

TRIS Rating considers PHATRA to be a core member of KKP Group, mainly because PHATRA generated an average of 18% of KKP’s average net profit over the past three years, which is considered to be a significant contribution to the overall performance of KKP. After becoming a wholly-owned subsidiary of KKP, PHATRA has been receiving both business and financial supports from KK and has been expanding its client base by leveraging KK’s client base, especially among high-net-worth clients. KK has been granting PHATRA a large credit line, which serves as an additional source of funds helping to enhance PHATRA’s financial flexibility.

Well-diversified sources of revenue

PHATRA’s revenue base is well-diversified. Brokerage fees represented 48% of total revenue in the first six months of 2017, compared with an industry average of 61% during the same period. Brokerage fees constituted 46% of total revenue in 2017. Less reliance on revenue from brokerage services makes the company’s earnings less susceptible to fluctuations in market trading volumes and to a decline in brokerage commission rates. Fees and service income accounted for 31% of total revenue in 2017, up from 18% in 2016. Meanwhile, gains on trading from its proprietary investments represented 6% of total revenue in 2017, a decrease from 19% in 2016.

For the securities brokerage business, PHATRA has a solid brokerage franchise for institutional investors. The company has distinguished itself by focusing its resources on providing services for institutional investors, both local and foreign. However, due to increasingly intense competition, PHATRA has experienced a decline in brokerage market share for foreign investors from 9.1% in 2016 to 7.5% in 2017 while market share for local institutions remained strong at 9.2% in 2017.

Potential growth in wealth management and strong track record in investment banking

PHATRA provides asset allocation advisory services to its high net worth clients with access to a wide variety of financial products from its open-architecture platform. The company's assets under advisement grew by 18%, from Bt379 billion in 2016 to Bt447 billion in 2017. By providing such value-added services, PHATRA avoids competing directly with other brokers based on commission rates alone. In addition, as a selling agent, PHATRA also earns recurring fees for the amounts of its clients' wealth invested in mutual funds run by other asset management companies.

PHATRA is one of the leading underwriters and financial advisors in the Thai capital market, with longstanding relationships with many large corporations. Its strong distribution channel, both in the local and international markets, along with its strong track record, should help it secure its leading market position. Revenue from investment banking has averaged Bt283 million a year over the past three years, or a market share of approximately 11%. In addition, with KKP as its ultimate parent company, PHATRA will be able to offer its clients a broader scope of financial solutions to serve their funding needs. The synergy will enhance PHATRA's strength in the investment banking business in the long run.

Limited exposure to both market and credit risk

PHATRA has been expanding its principal investment activities. Even though PHATRA is pursuing supposedly low-risk trading strategies and has no positions that closely track market direction, its risk profile is affected by the expansion of these inherently risky activities. Nonetheless, TRIS Rating expects PHATRA to maintain an adequate risk management system to cover its principal investment activities.

As of December 2017, PHATRA had no classified receivables. PHATRA does not engage in margin lending. Therefore, its credit risk is only limited to the risk incurred when providing brokerage services.

Profitability in line with peers and relatively low operating costs

The inherently cyclical nature of the securities industry contributes to volatile profitability for securities companies, including PHATRA. Net profit dropped by 11% from 2016 to Bt738.1 million in 2017. The decline was due to a slightly lower brokerage fee from the securities segment and lower gains on trading. The company's ratio of return on average assets (ROAA) on a non-annualized basis was 1.44% in the first six months of 2017, compared with the industry average of 1.63%. The ratio was 3.5% in 2017. PHATRA's operating expenses are low relative to its peers. The ratio of operating expenses to net revenue was 56.7% in the first six months of 2017, compared with the industry average of 64.5%. The ratio was 55% in 2017.

Sufficient liquidity and strong equity base

PHATRA has a large number of credit lines available through credit facilities from several financial institutions. The amount of total credit should be enough to fund the company's operations and cover any liquidity shortfalls. After merging with KK, PHATRA was granted a credit facility in an amount not exceeding 25% of KKP's capital fund of solo consolidation group to be shared with the affiliated companies within Capital Market Group. This source of funds has further enhanced PHATRA's financial flexibility. PHATRA's issuance of financial products, such as structured notes, has also served as an additional source of funds.

As of December 2017, PHATRA's shareholders' equity stood at Bt5,653 million, one of the highest equity bases among its peers. Despite the large capital base, PHATRA is one of the most highly-leveraged securities firms. The company's ratio of equity to adjusted assets was 43.7% in the first six months of 2017, compared with the industry average of 57.9%. The ratio was 39.7% in 2017. The rise in PHATRA's financial leverage in the last few years was due to the expansion of its proprietary investment portfolio and hedging activities related to financial products issued for clients. PHATRA ended 2017 with a net capital ratio (NCR) of 32%, higher than the regulatory requirement of 7%.

RATING OUTLOOK

The "positive" outlook reflects an improvement of KK's credit profile and the credit linkage between KK and PHATRA.

RATING SENSITIVITIES

The rating and/or outlook of PHATRA could be revised upward or downward should there be any changes in KK's credit profile or if there are any changes in PHATRA's status relative to other subsidiaries or affiliates of KK.

COMPANY OVERVIEW

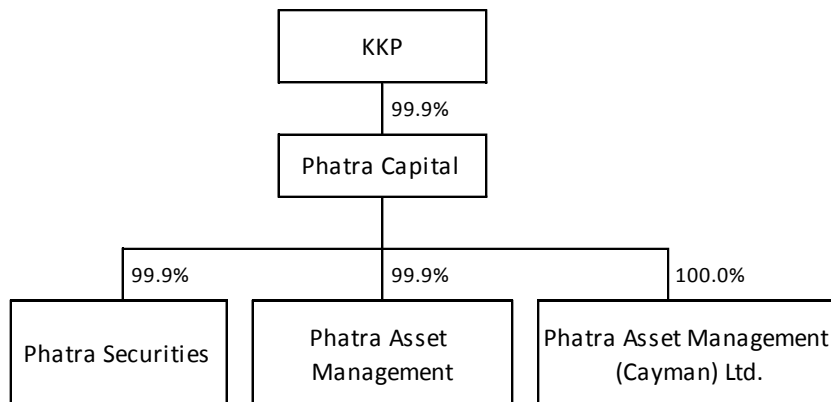
PHATRA was spun off from Phatra Thanakit in 1997, becoming a 99.99% owned subsidiary of Phatra Thanakit. Prior to the spin-off, its securities business had been conducted as a department within Phatra Thanakit since 1975. In 1998, PHATRA

changed its name to Merrill Lynch Phatra Securities Co. after Merrill Lynch & Co. (ML) and Kasikorn Bank (KBANK) acquired 51% and 49% stakes in PHATRA, respectively. The company changed its name back to Phatra Securities when ML and KBANK sold their combined stakes in Merrill Lynch Phatra Securities to the current management team, employees, and selected investors in 2003. PHATRA became a public company and its shares were listed on the Stock Exchange of Thailand (SET) in 2005.

PHATRA has collaborated with ML since 2003. The alliance covers research, securities brokerage, and investment banking. In 2010, the company restructured. Phatra Capital was set up as a holding company and the Direct Investment (DI) portfolio was transferred from Phatra Securities to the newly set-up Phatra Capital. Phatra Capital was listed on the SET in place of Phatra Securities. The restructuring had three goals: to separate the risks of the agency business and the principal investment business, to give PHATRA more flexibility for future expansion efforts and strategic partnership opportunities, and to minimize conflicts of interest between the agency and principal investment businesses.

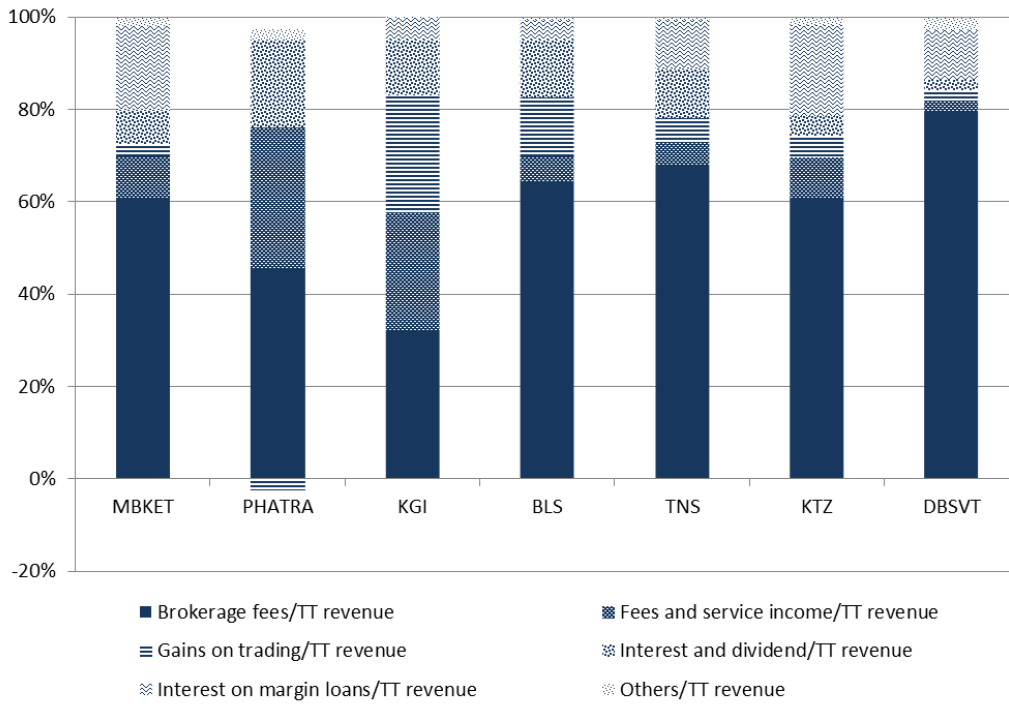
As of May 2015, Phatra Capital held a 99.9% stake in Phatra Securities. Before the merger with KKP, PHATRA's expansion efforts were constrained by limitations on capital, size, and business scope inherent in PHATRA's securities business license. The development of, and competition in, the country's and the region's financial markets threatened PHATRA's long-term competitive position. As a result, in April 2012, PHATRA's shareholders approved the merger with KKP at the annual general meeting. In September 2012, the merger was successfully completed. KKP now holds 99.9% of Phatra Capital.

Chart 1: KKP Group Structure as of Dec 2017



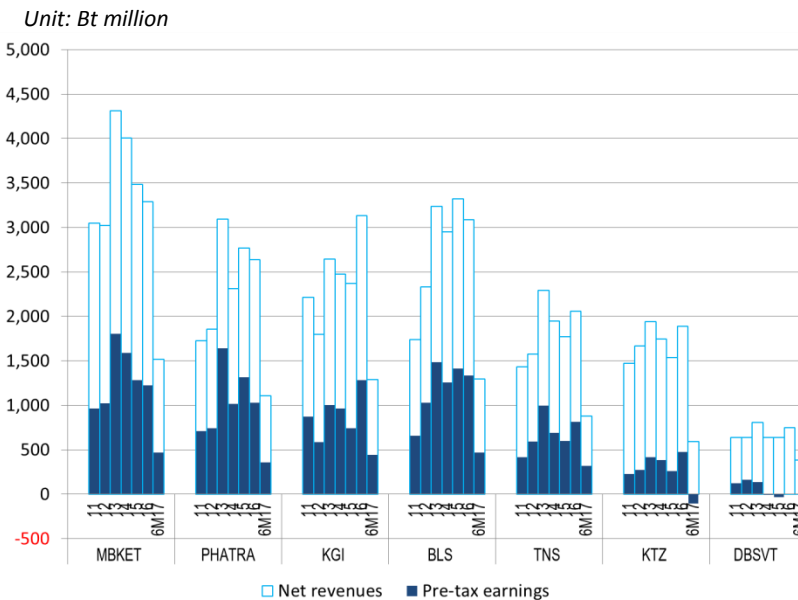
KEY OPERATING PERFORMANCE

Chart2: Revenue Structure in 1H2017 (Jan-Jun 2017)



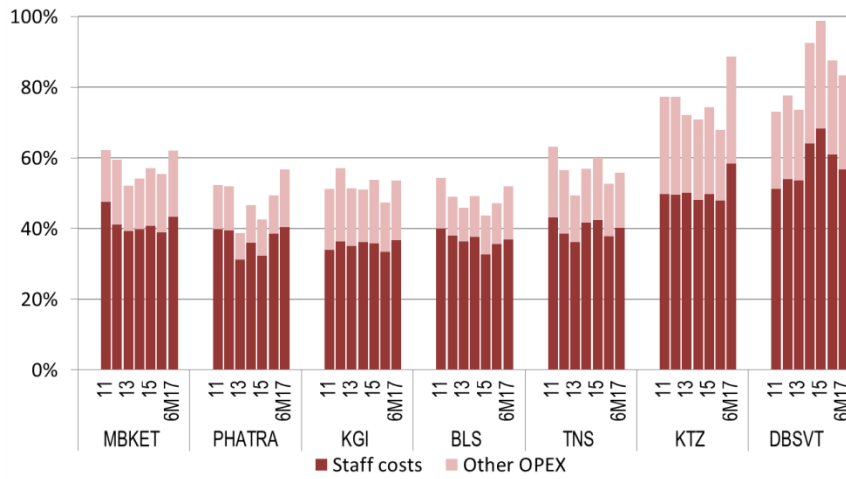
Source: Financial statements of each company

Chart 3: Net Revenues and Pre-tax Earnings of Selected Brokers in 2011 – 1H2017



Source: Financial statements of each company

Chart 4: 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	20,750	21,506	21,122	16,614	18,232
Net Investment in securities	10,727	11,574	4,024	4,801	6,413
Total securities business receivables and accrued interest receivables	4,741	7,593	14,279	7,018	9,788
Allowance for doubtful accounts	-	-	-	-	-
Total debts*	8,154	6,978	3,330	2,409	2,333
Shareholders' equity	5,653	5,799	6,007	5,260	4,961
Net securities business income	2,312	2,256	2,409	2,061	2,803
Total income	2,803	2,748	2,850	2,416	3,185
Operating expenses	1,459	1,306	1,176	1,078	1,199
Interest expenses	151	108	82	103	92
Net income	738	828	1,052	811	1,309

* Including structured notes

Unit: %

	----- Year Ended 31 December -----				
	2017	2016	2015	2014	2013
Profitability					
Brokerage fees/total revenues	45.7	49.3	47.8	57.5	56.5
Fees and services income/total revenues	31.5	18.2	10.1	8.2	19.7
Gain (loss) from trading/total revenues	5.6	18.9	28.3	22.1	15.0
Operating expenses/net revenues	55.0	49.5	42.5	46.6	38.8
Pre-tax margin	35.1	39.1	47.7	43.9	53.0
Return on average assets	3.5	3.9	5.6	4.7	9.2
Return on average equity	12.9	14.0	18.7	15.9	30.4
Asset Quality					
Classified receivables/gross securities business receivables	0.0	0.0	0.0	0.0	0.0
Allowance for doubtful accounts/gross securities business receivables	0.0	0.0	0.0	0.0	0.0
Credit costs	0.0	0.0	0.0	0.0	0.0
Capitalization					
Equity/Adjusted assets	39.7	36.3	44.3	45.8	31.6
Liquidity					
Liquid assets/total assets	54.5	57.9	21.4	38.3	39.7
Liquid assets/adjusted assets	79.5	77.9	33.6	55.4	46.1
Less liquid assets/long-term capital	4.4	4.9	4.8	5.5	5.8

Phatra Securities PLC (PHATRA)

Company Rating:

A-

Rating Outlook:Positive

TRIS Rating Co., Ltd.

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

© Copyright 2018, TRIS Rating Co., Ltd. All rights reserved. Any unauthorized use, disclosure, copying, republication, further transmission, dissemination, redistribution, or storing for subsequent use for any purpose, in whole or in part, in any form or manner or by any means whatsoever, by any person, of the credit rating reports or information is prohibited, without the prior written permission of TRIS Rating Co., Ltd. The credit rating is not a statement of fact or a recommendation to buy, sell or hold any debt instruments. It is an expression of opinion regarding credit risks for that instrument or particular company. The opinion expressed in the credit rating does not represent investment or other advice and should therefore not be construed as such. Any rating and information contained in any report written or published by TRIS Rating has been prepared without taking into account any recipient's particular financial needs, circumstances, knowledge and objectives. Therefore, a recipient should assess the appropriateness of such information before making an investment decision based on this information. Information used for the rating has been obtained by TRIS Rating from the company and other sources believed to be reliable. Therefore, TRIS Rating does not guarantee the accuracy, adequacy, or completeness of any such information and will accept no liability for any loss or damage arising from any inaccuracy, inadequacy or incompleteness. Also, TRIS Rating is not responsible for any errors or omissions, the result obtained from, or any actions taken in reliance upon such information. All methodologies used can be found at www.trisrating.com/rating-information/rating-criteria