

RHB SECURITIES (THAILAND) PLC

No. 56/2019
26 April 2019

FINANCIAL INSTITUTIONS

Company Rating: AA-
Outlook: Stable

Last Review Date: 14/03/18

Company Rating History:

Date	Rating	Outlook/Alert
14/03/18	AA-	Stable

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RATIONALE

TRIS Rating affirms the company rating on RHB Securities (Thailand) PLC (RHBS) at “AA-” with a “stable” outlook. RHBS’s rating is enhanced from its stand-alone credit profile to reflect its status as a highly strategic subsidiary of RHB Bank Berhad (RHB Bank) (“AA/Stable”), Malaysia’s fourth largest banking group. The stand-alone credit profile is based on the company’s sufficient liquidity and capital base and its limited exposure to market and credit risk. However, the rating is constrained by its weak financial performance and its reliance on brokerage fees as a main revenue source.

KEY RATING CONSIDERATIONS

A highly strategic subsidiary of RHB Bank Group

RHBS is considered RHBS a highly strategic subsidiary of the RHB Bank Group (comprising RHB Bank and all subsidiaries) as the company is 99.9% owned by RHB Investment Bank Berhad (RHBIB), which in turn is wholly-owned by and a core subsidiary of RHB Bank. RHBS serves as a part of RHB Bank Group’s regional franchises in Asia and has continued to receive both business and financial support from the RHB Bank Group. The company also operates under the group’s integrated risk management systems and operating platforms and has been granted credit facilities from the group, which has helped to enhance the company’s financial flexibility.

Sufficient liquidity and capital base

TRIS Rating expects RHBS to have sufficient liquidity to cover any temporary liquidity shortfall at the current scale of operations, as the company has available credit facilities from several financial institutions in addition to the credit lines available from RHB Bank (Bangkok Branch).

RHBS’s capital base was also large enough to absorb losses from the credit risk of its margin loan portfolios and the market risk of its investment portfolios. As of June 2018, the company’s ratio of equity to adjusted assets, a measure of financial leverage, was 58.2%, relatively in line with the industry average of 54.2%. RHBS ended 2018 with a net capital ratio (NCR) of 52%, compared with 54% a year earlier and the regulatory requirement of 7%.

Tightened risk management helps limit exposure to market and credit risk

RHBS’s exposure to market risk is manageable as its proprietary trading activities are only limited to the hedging of its positions in financial products offered by the company.

RHBS’s outstanding margin loans remained at Bt1.4 billion at end-2018, representing 2.3% of industry-wide margin lending and 0.9 times RHBS’s equity. The size of margin loans declined from Bt2.2 billion at end-2017, as the company scaled back its margin lending business as a result of risk management enhancements following its loss experience in the first half of 2017 (1H2017). TRIS Rating believes that the company’s tightened risk management systems and credit control policies, in addition to its compliance to the risk management policies of RHB Bank group, should help limit its credit risks.

Weak financial performance

Fierce competition in the industry and the company’s high operating costs continue to put a strain on its financial performance. The company reported a

net loss of Bt127.6 million in 2018, compared with a net loss of Bt80 million in 2017. RHBS's annualized return on average assets (ROAA) was -1.6% for the first six months of 2018, lower than the industry average of 4.3%. A decrease in fees and service income, mainly from underwriting and financial advisory fees, and a decline in gains on trading were the main contributors to the decrease in the company's total revenue in 2018. Nevertheless, we expect revenues from these two sources to improve over the next few years as the company has recruited an experienced investment banking team and plan to expand its product offerings, which should help strengthen its earnings over the next few years.

Meanwhile, RHBS has also experienced downward pressure on its earnings from brokerage fees. The company's revenue shares in securities brokerage decreased slightly to 1.3%, ranking 25th for the first six months of 2018, down from 1.6% or 23rd in 2017, due mainly to lower market share in trading volume and brokerage commission. Although its average commission rates were below an industry average of 10 basis points (bps) in 2018, we expect RHBS's average commission rate to maintain at the current level for the company to sustain its earnings from its brokerage business.

In addition to lower revenue generation, RHBS's high operating expenses has put additional pressure on the company's profitability. The company's ratio of operating expenses to net revenues was 94.5% for the first six months of 2018, higher than the industry average of 59.8%. We project RHBS's ratio of operating expenses to net revenue to be in a range of 80%-85% over the next few years, as revenues are expected to increase.

Reliance on brokerage fees

RHBS's reliance on securities brokerage fees as its predominant source of income means that its revenue is subject to market volatility as well as intense competition after the liberalization of brokerage commissions. Brokerage fees constituted 61.1% of total revenue in the first six months of 2018, although this is in line with the industry average of 61.5%. Retail clients, which are more price sensitive relative to institutional clients, accounted for 86.5% of the company's trading volume in 2018.

At the same time, contributions from other revenue sources remain limited. Fees and service income accounted for 3.8% of total revenue in the first six months of 2018, lower than the industry average of 12.0%. Its gains on trading also shrank in 2018, constituting 9.0% of total revenue in 2018 down from 16.8% in 2017, partly due to the scaling down of investment activities for hedging after the loss experience in 1H2017. As the company plans to improve and expand product offerings, e.g. derivatives products, we expect the strategy to help diversify RHBS's revenue mix over the next few years.

BASE-CASE ASSUMPTIONS IN 2019-2021

- Average commission rate to maintain approximately at the current level.
- Operating expense to net revenue to range between 80%-85%.
- Return on average assets to range between 0%-2%.

RATING OUTLOOK

The "stable" outlook reflects our view that RHBS will maintain its status as a highly strategic subsidiary of the RHB Bank Group and continue to operate as an integral part of the group.

RATING SENSITIVITIES

The rating and/or outlook of RHBS could be revised upward or downward should there be any changes in RHB Bank Group's credit profile or if TRIS Rating perceives any significant changes in the degree of support RHBS receives from the RHB Bank Group or if there are any changes in RHBS's status relative to other subsidiaries or affiliates of the RHB Bank Group.

COMPANY OVERVIEW

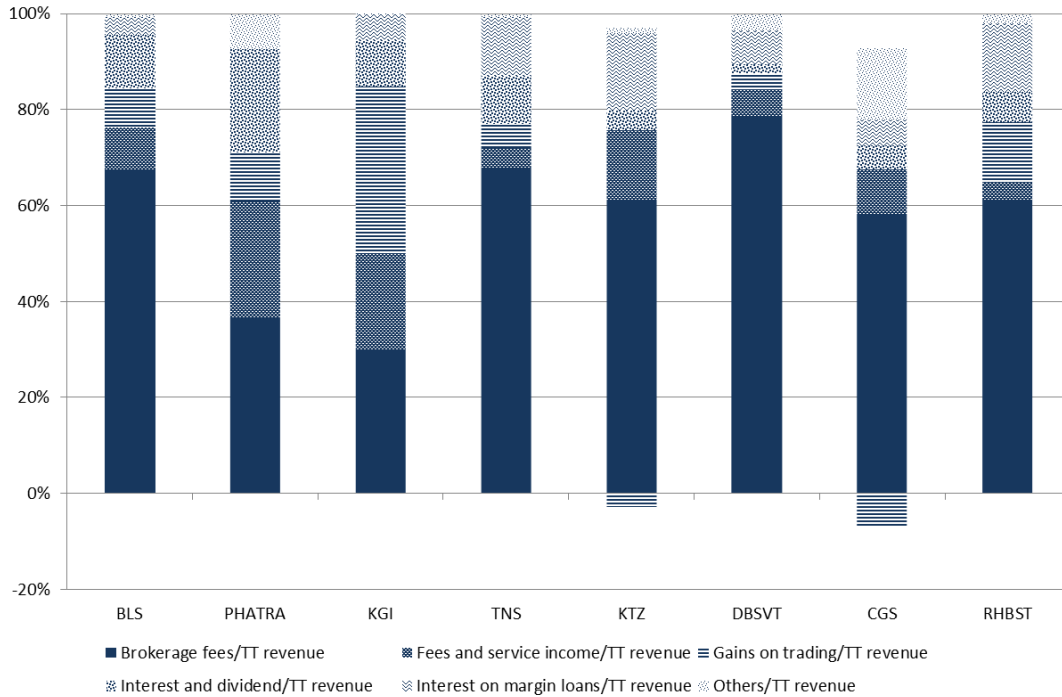
RHBS is 99.9% owned by RHB Investment Bank Berhad (RHBIB), a wholly-owned investment banking arm of RHB Bank. RHB Bank is the fourth largest commercial bank by asset size among the total eight local banks in Malaysia. Apart from commercial banking and investment banking businesses, the RHB Bank Group also has significant operations in insurance and asset management businesses through its subsidiaries, which altogether referred to as the RHB Bank Group. RHB Bank is rated "AA" with a "stable" outlook by TRIS Rating, and is rated "BBB+" with a "stable" outlook by S&P Global Ratings. RHBIB receives the same rating and outlook from S&P Global Ratings, reflecting its status as a "core" subsidiary of the RHB Bank.

RHBS was established in 2000 as BFIT Securities PLC, and was listed on the Stock Exchange of Thailand (SET) in 2004. In

2011, the company was renamed OSK Securities (Thailand) PLC, after OSK Investment Bank Berhad, Malaysia, acquired a 49.8% equity stake in the company. In 2013, the company was delisted from the SET after RHB Capital Berhad became its major shareholder. In 2015, following an internal restructuring at the RHB Group level, the company was renamed RHB Securities (Thailand) PLC. With the operational integration which started in 2014, RHBS now operates as part of RHBIB's operating platform with integrated risk management and control.

KEY OPERATING PERFORMANCE

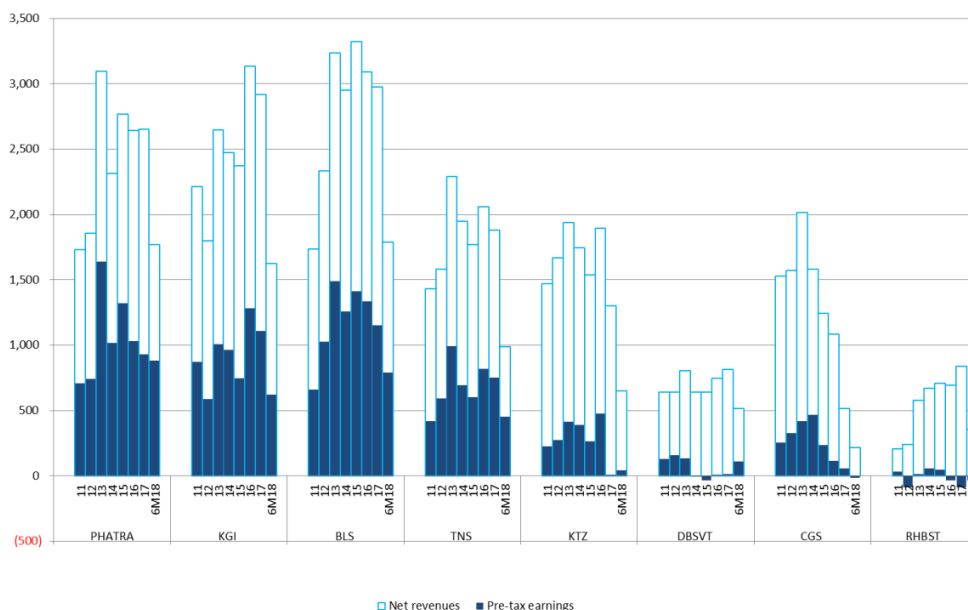
Chart 1: Revenue Structure in 1H2018 (Jan-Jun 2018)



Source: Financial statements of each company

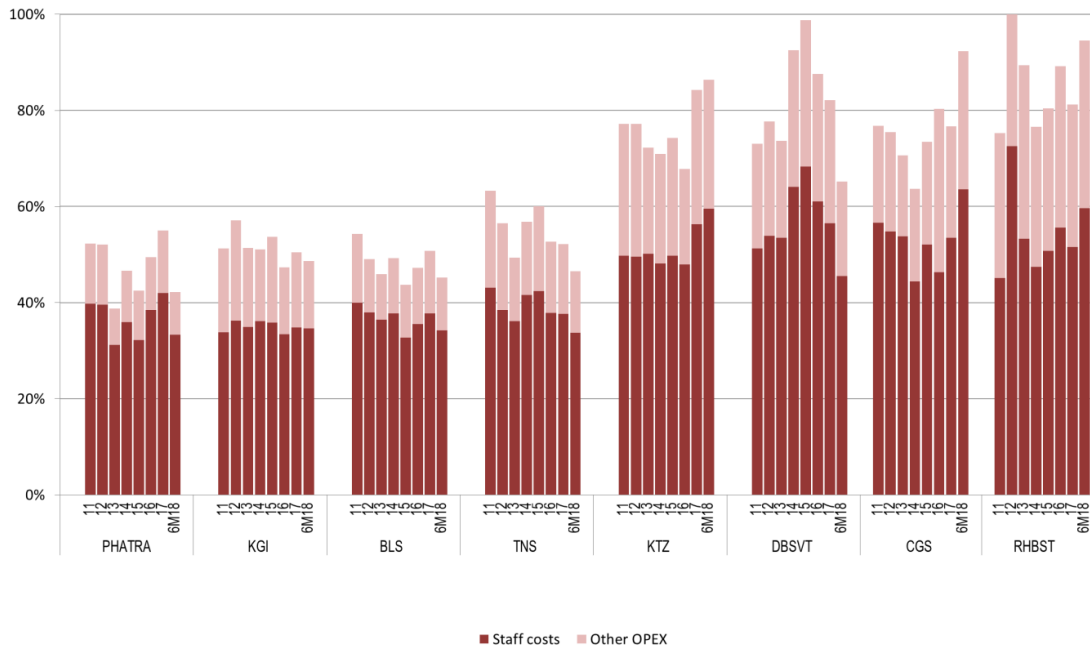
Chart 2: Net Revenues and Pre-tax Earnings of Selected Brokers in 2011-1H2018

Unit: Bt million



Source: Financial statements of each company

Chart 3: Staff Cost and Other Operating Expenses of Selected Brokers in 2011-1H2018 (% of Net Revenues)



Source: Financial statements of each company

- Notes:
- PHATRA = Phatra Securities PLC
 - KGI = KGI Securities (Thailand) PLC
 - BLS = Bualuang Securities PLC
 - TNS = Thanachart Securities PLC
 - KTZ = KT ZMICO Securities Co., Ltd.
 - DBSVT = DBS Vickers Securities (Thailand) Co., Ltd.
 - CGS = Country Group Securities PLC
 - RHBST = RHB Securities (Thailand) PLC

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS
Unit: Bt million

	-----Year Ended 31 December -----				
	2018	2017	2016	2015	2014
Total assets	4,449	5,266	6,081	4,693	4,438
Net Investment in securities	521	863	1,821	649	1,188
Total securities business receivables and accrued interest receivables	2,249	3,467	2,721	2,296	2,141
Allowance for doubtful accounts	127	127	0	0	0
Total debts	1,750	1,790	2,584	1,366	1,636
Shareholders' equity	1,907	2,025	2,105	2,135	2,085
Net securities business income	492	708	571	595	572
Total income	684	926	750	774	735
Operating expenses	633	680	612	571	514
Interest expenses	69	88	58	64	64
Net income	(128)	(80)	(30)	41	63

Unit: %

	-----Year Ended 31 December -----				
	2018	2017	2016	2015	2014
Profitability					
Brokerage fees/total revenues	61.1	50.8	52.1	43.1	49.1
Fees and services income/total revenues	4.7	10.2	4.2	6.7	6.2
Gain (loss) from trading/total revenues	9.0	16.8	20.0	16.6	18.2
Operating expenses/net revenues	103.1	81.2	88.4	80.4	76.6
Pre-tax margin	(20.4)	(10.7)	(4.9)	6.3	11.8
Return on average assets	(2.6)	(1.4)	(0.6)	0.9	1.7
Return on average equity	(6.5)	(3.9)	(1.4)	2.0	3.1
Asset Quality					
Classified receivables/gross securities business receivables	5.7	3.7	0.0	0.0	0.1
Allowance for doubtful accounts/gross securities business receivables	5.7	3.7	0.0	0.0	0.0
Credit costs (reversal)	0.0	4.2	0.0	(0.1)	0.0
Capitalization					
Equity/adjusted assets	54.1	52.0	47.5	66.4	58.3
Liquidity					
Liquid assets/total assets	43.0	28.8	35.7	29.5	39.1
Liquid assets/adjusted assets	54.3	38.9	49.0	43.1	48.5
Less liquid assets/long-term capital	76.1	111.8	102.2	79.0	80.3

RELATED CRITERIA

- Securities Company in Thailand, 21 December 2017
- Group Rating Methodology, 10 July 2015

RHB Securities (Thailand) PLC (RHBS)

Company Rating:	AA-
Rating Outlook:	Stable

TRIS Rating Co., Ltd.

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