

THANACHART BANK PLC

No. 31/2020
19 March 2020

FINANCIAL INSTITUTIONS

Company Rating:	AA-
Issue Ratings: Basel III tier-II	A
Outlook:	Stable

Last Review Date: 10/10/19

Company Rating History:

Date	Rating	Outlook/Alert
16/01/12	AA-	Stable
12/03/10	A+	Positive
04/04/08	A+	Stable
14/07/05	A	Stable

Contacts:

Annop Supachayanont, CFA
annop@trisrating.com

Preeyaporn Kosakarn
preeyaporn@trisrating.com

Jittrapan Pantaleard
jittrapan@trisrating.com

Narumol Charnchanavivat
narumol@trisrating.com



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RATIONALE

TRIS Rating affirms the company rating on Thanachart Bank PLC (TBANK) at “AA-” and affirms the rating on the bank’s Basel III tier-II capital securities at “A” with a “stable” outlook.

The ratings are underpinned by TBANK’s strong business position which has been supported by its unwavering strength in the auto finance value chain. The rating also takes into account the bank’s adequate capital position. We assess TBANK’s current funding and liquidity profile at an average level compared with overall banking peers. We also hold the view that TBANK’s risk position remains well under control.

The merger between TBANK and TMB Bank PLC (TMB) could provide prospects for future business expansion for both banks. However, the integration risks and unfavourable economic conditions continue to weigh on TBANK’s rating.

KEY RATING CONSIDERATIONS

Solid auto franchise

One of the credit factors that have underpinned TBANK’s rating is its solid market position in Thailand’s auto loan market. TBANK’s financing capability covers the entire value chain from automakers to auto dealers and retail consumers. In the retail space, the bank has maintained the highest market share of over 20% among auto hire-purchase lenders, based on our data¹.

TBANK is transitioning towards an entire business transfer (EBT) scheduled for July 2021 during which TBANK will transfer all assets and liabilities to TMB and enter the liquidation process. Currently, both banks are still operating as two separate legal entities under a single board and joint management team.

From now until the EBT, both banks are working on combining their respective customer bases and aligning products and service channels via joint brand and co-location. For example, on the retail front, TBANK’s auto loan and title loan products will be offered to TMB’s customers, while TMB’s low-cost deposit products will be offered to TBANK’s customers. This and other areas of the integration process should help strengthen TBANK’s business position and earnings in the longer term.

Strong capital

We assess TBANK’s stand-alone capital position as being strong, with CET-1 at 17.66% at the end of 2019. Its capital quality is also viewed as being strong, compared with the average level for most banks, considering its CET-1 capital was above 85% of total capital as of end-2019. We expect TBANK to maintain a strong capital position in 2020, based on our assumption that the dividend payout will be in its normal range of 40% and loan growth will still be in the single-digit range. The CET-1 capital ratio disclosed by TMB at end-2019, with TBANK consolidated, stood at 13.62%.

Satisfactory funding and liquidity profiles

TBANK’s current funding position is considered average compared with banking peers. The bank’s stable funding at end-2019 comprised 81.7% deposits and 3.5% borrowings (excluding interbank). The total capital fund of Bt133 billion

¹ These are commercial banks and non-bank financial institutions, including leasing companies.

made up the remaining 14.8% of stable funds.

Total deposits as of end-2019 included 52% current accounts and savings accounts (CASA) deposits, 37% fixed deposits and 11% certificate of deposits. Approaching the EBT, TBANK's deposit base will gradually contract due to the migration plan where TBANK will start offering TMB's deposit products to its customers. In terms of borrowings, the bank has outstanding short-term debentures of Bt12.8 billion, all of which mature in March 2020. The bank plans to replace these with new instruments to be issued under TMB's name. TBANK also has Basel III Tier-2 instrument of Bt7 billion, with a call option in the fifth year in May 2020, which is also expected to be called.

TBANK's liquidity, measured by liquid assets to total deposits, stood at a comfortable 35% at the end of 2019. Prior to the merger and acquisition (M&A), the liquidity coverage ratio (LCR) stood at 127% at the end of the first half of 2019, compared with the average for Thai banks of 179%. These levels were above the regulatory requirement of 90%.

Improved financial performance

TBANK reported consolidated net profit of Bt26.4 billion in 2019, a 70% increase from 2018. The main driver was the gain of Bt3.86 billion recognized on TBANK's divestment of various subsidiaries and related companies as part of the group restructuring. Excluding this amount, net profit remained strong, improving by 8% year-on-year (y-o-y). Return on average assets (ROAA), excluding the gain, was 1.6% compared with 1.5% in 2018. This is despite the higher loan loss provision and income taxes in 2019. The bank's operating performance improved from 2018 mainly due to higher total revenue and stable operating costs. Risk-adjusted net interest margin rose marginally to 2.39% from 2.37% in 2018, thanks to stronger loan yield, particularly yield on auto hire purchase loans, in spite of higher funding costs.

Risk position remains manageable

Gross loans declined by 4% y-o-y from end-2018 with no sign of significant change in exposure. Auto hire purchase and housing loans grew at a healthy pace of 7% and 4%, respectively, while most other segments contracted. During the transition, auto loans (including hire purchase and title loans) will continue to be booked on TBANK's balance sheet. However, other types of loans may be booked either at TBANK or TMB depending on products offering and loan origination. This is likely to result in further contraction of TBANK's loan portfolio. The change in loan origination and the funding migration also means that TBANK's financial performance in 2020 may not be comparable to that of 2019.

Meanwhile, overall asset quality weakened modestly, with the bank-only classified non-performing loan (NPL) ratio increasing to 2.7% in 2019 from 2.5% at end-2018. The sectors that deteriorated include manufacturing and commerce, real estate and construction, and auto hire purchase. Nonetheless, the NPL ratio of hire purchase loans remained manageable at 1.3%. Credit cost in 2019 widened marginally to 0.74% from 0.61% in 2018, but remained well within its normalized level and significantly below banking peers.

Basel III tier-II securities

The "A" rating on TBANK's outstanding Basel III tier-II capital securities (TBANK25NA) reflects the subordination and the non-payment risk of the securities, as defined by the non-viability loss absorption clause. The features of the securities comply with the Basel III guidelines and the securities are qualified as tier-II capital under the Bank of Thailand's (BOT) criteria. The issues are subject to full or partial write down of principal in the event that the regulator deems the bank to be non-viable and decides to provide financial support to the bank. The holders of the securities are subordinate to TBANK's depositors and holders of TBANK's senior unsecured debentures. The issues are callable by TBANK in the fifth year in May 2020, subject to approval from the BOT.

RATING OUTLOOK

The "stable" outlook reflects our foreseeable view that TBANK will maintain its strength in auto lending, adequate capital, and good asset quality.

RATING SENSITIVITIES

TBANK's ratings may be upgraded if there are evidences of successful integration between TBANK and TMB and benefits are forthcoming from synergy of the merged banks. The evidences may include improved core profitability of the combined bank, with overall risk position remaining prudent. At the same time, the consolidated CET1 of the merged bank should sustain above 14.5%. Unsuccessful integration, resulting in a deteriorating risk position of the combined bank as well as weakening profitability and capital on a sustained basis may lead to a rating downgrade for TBANK.

COMPANY OVERVIEW

TBANK was established as a result of the merger of Ekachart Finance PLC and other financial institutions. After receiving a commercial bank license from the Ministry of Finance (MOF), the bank commenced operations, with paid-up capital of Bt8.1 billion, in April 2002, and became a universal bank under a full banking license in March 2004.

Thanachart Capital PLC (TCAP), formerly named National Finance PLC, together with TBANK, submitted a reorganization plan for the Thanachart Group to the MOF in mid-2004. TCAP transferred its businesses to TBANK and became a non-operating holding company of TBANK. In July 2007, TCAP signed a joint-venture agreement with Bank of Nova Scotia (BNS), a new Canadian strategic partner. As a consequence, TBANK had two major shareholders, with TCAP holding 51% while BNS held a 49% stake.

In March 2010, TBANK acquired Siam City Bank (SCIB) and established TS Asset Management to manage SCIB's non-performing assets. In October 2011, TBANK also injected new capital into Ratchthani Leasing PLC (THANI), to increase its stake to 65% from 48%. Later, in May 2013, TBANK sold Thanachart Life Insurance to Prudential Life Assurance (Thailand) PLC for approximately Bt17.5 billion in exchange for a 15-year exclusive bancassurance partnership.

In October 2015, TBANK issued a rights offering to existing shareholders of Bt5.5 billion for use in redeeming its hybrid tier-I capital of Bt7.1 billion. TBANK's total issued and paid-up capital increased to Bt60.6 billion.

On 26 February 2019, the five parties including TMB, TBANK, TCAP, ING Groep N.V. (ING), and BNS signed an agreement to merge TMB and TBANK. As the merger focuses on TBANK's banking business, TBANK was required to divest its holdings in its subsidiaries and other investments to TBANK's shareholders based on the respective shareholdings (TCAP 51%; BNS 49%). The subsidiaries include Thanachart Securities PLC, THANI, Thanachart Insurance PLC, and TS Asset Management Co., Ltd.

In December 2019, TMB and TBANK completed the share purchases and TBANK became a wholly-owned subsidiary of TMB. As of end-2019, TCAP held a 20.1% share in TMB. Other shareholders of TMB included ING (23.0%), MOF (11.8%), Vayupak Fund 1 (9.9%), BNS (5.9%), and others (29.3%). TBANK will continue to operate as a separate legal entity until the EBT takes place in July 2021, after which TBANK will enter a liquidation process.

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS¹

Unit: Bt million

	-----Year Ended 31 December -----				
	2019	2018	2017	2016	2015
Total assets	1,003,720	1,046,612	1,009,557	950,512	980,972
Average assets	1,025,166	1,028,084	980,034	965,742	994,931
Investment in securities	110,018	163,515	169,626	177,334	173,682
Loans and receivables	714,575	754,143	712,264	691,527	714,124
Allowance for doubtful accounts	20,046	23,652	24,034	24,618	25,680
Deposits	734,352	752,160	716,278	676,557	669,504
Borrowings ²	78,104	115,034	121,732	115,243	157,329
Shareholders' equities	163,260	144,205	136,208	126,121	117,691
Average equities	153,733	140,207	131,164	121,906	111,928
Net interest income	29,400	31,038	29,410	28,712	27,681
Non-interest income ³	11,845	12,201	12,572	11,695	12,201
Total revenue	41,245	43,239	41,982	40,407	39,882
Operating expenses	18,605	20,525	20,437	20,626	19,964
Pre-provision operating profit (PPOP)	22,639	22,714	21,545	19,781	19,917
Impairment losses on loans and securities	5,439	4,741	6,244	6,251	8,592
Net income	26,370	15,458	14,369	12,839	11,127
Net fee and service income	4,974	6,627	5,897	5,904	5,475
Gains on investments	4,528	(85)	1,113	714	1,533

1 Consolidated financial statements

2 Including interbank and money market

3 Including net insurance income

Unit: %

	-----Year Ended 31 December -----				
	2019	2018	2017	2016	2015
Earnings					
Return on average assets	2.57	1.50	1.47	1.33	1.12
Interest spread	2.63	2.81	2.80	2.76	2.54
Net interest margins	2.93	3.08	3.07	3.04	2.85
Net interest income/average assets	2.87	3.02	3.00	2.97	2.78
Non-interest income/average assets	1.16	1.19	1.28	1.21	1.23
Net fee and service income ³ /total revenue	12.06	15.33	14.05	14.61	13.73
Cost-to-income	45.11	47.47	48.68	51.04	50.06
Capitalization					
CET-1 ratio ⁴	17.66	15.42	14.81	13.27	12.04
Tier-1 ratio ⁴	17.66	15.42	14.81	13.27	12.04
BIS ratio ⁴	19.65	19.45	18.94	19.15	17.92
CET-1/BIS ratio ⁴	89.84	79.24	78.24	69.30	67.18
Asset Quality					
Credit costs	0.74	0.65	0.89	0.89	1.17
Non-performing loans/total loans ⁵	2.27	2.27	2.25	2.23	2.81
Non-performing assets/total assets	3.02	2.87	2.98	3.40	4.16
Allowance for loan losses/non-performing loans	102.45	122.36	132.72	149.79	109.92
Funding & Liquidity					
CASA/total deposits	51.53	48.52	42.93	45.58	40.14
Loan/total deposits	97.23	100.26	99.44	102.21	106.66
Deposits/total liabilities	87.37	83.35	82.02	82.07	77.55
Liquid assets/total deposits ⁶	33.77	32.72	34.24	31.61	32.14
Liquid assets/short-term financial liabilities ⁷	33.29	34.24	32.31	29.29	28.97

3 Including net insurance income

4 Consolidated basis

5 Including interbank; excluding accrued interests

6 Including interbank borrowing

7 Financial liabilities with maturity less than one year

RELATED CRITERIA

- Banks Rating Methodology, 3 March 2020

- Group Rating Methodology, 10 July 2015

Thanachart Bank PLC (TBANK)

Company Rating:

AA-

Issue Rating:

TBANK25NA: Bt7,000 million Basel III tier-II capital securities due 2025

A

Rating Outlook:

Stable

TRIS Rating Co., Ltd.

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

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