

TSFC SECURITIES PLC

 No. 231/2021
 30 December 2021

FINANCIAL INSTITUTIONS

Company Rating: BBB
Outlook: Stable

Last Review Date: 28/12/20

Company Rating History:

Date	Rating	Outlook/Alert
27/12/19	BBB	Stable
25/11/15	BBB-	Stable
04/12/14	BB+	Positive
26/10/12	BB+	Stable
15/08/12	BB+	Alert Developing
04/02/11	BB+	Positive
28/07/09	BB	Stable
17/12/08	D	
16/12/08	C	Alert Negative
28/11/08	BB-	Alert Negative
07/11/08	BBB-	Alert Negative
04/04/05	A	Stable
12/07/04	A-	Positive
09/05/02	A-	-

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RATIONALE

TRIS Rating affirms the company rating on TSFC Securities PLC (TSFC) at “BBB” with a “stable” rating outlook. The rating reflects the company’s moderate business position, strong capital, strong risk position, and manageable funding and liquidity profile.

KEY RATING CONSIDERATIONS

Moderate business position

The company’s business position has continued to be supported by its unique role as the only securities finance company (SFC) in Thailand with the mission to provide liquidity for securities firms and to act as a supporting arm to help with the development of Thai capital markets. At the end of September 2021, the company’s loans provided to brokers stood at THB840 million, an increase from THB600 million at the end of September 2020.

The company’s strong market presence in its main business of credit balance financing (margin lending), has also continued to underpin its business position. At the end of June 2021, the company ranked 7th in terms of credit balance outstanding with a share of 4.6%, a slight drop from 5th and 6th places over the previous few years. The company’s outstanding margin loans averaged around THB4 billion during the first nine months of 2021 (9M21), an increase by approximately 60% from 9M20. The increase is of smaller magnitude compared with the 103% increase of the industry’s average. This was due to the company’s reliance on brokers to supply margin loan volume, which limits its capacity to expand as opposed to direct approaches to clients. Nonetheless, we expect the company’s portfolio to gradually expand over the next few years. The company plans to enhance its promotional campaigns to encourage more client referrals from brokers and develop new product offerings to attract both retail and wholesale clients.

The company’s revenue sources are highly concentrated on interest income on margin loans. This continues to pressure its business position as we view TSFC’s revenue base as potentially being susceptible to declines in demands for margin loans due to shifts in product preference. For 9M21, interest income on margin loans contributed 89% of total revenue. Interest income on brokers’ loans represented another 9%, while fee-based income remained limited. In our view, an improvement in TSFC’s business position that could lead to a positive rating action will require a meaningful diversification of its revenue mix.

Strong capital

The company’s rating is supported by its strong capital as measured by a risk-adjusted capital ratio (RAC), which we forecast to stay at around 19% over the next few years. We expect the company’s capitalization to remain strong over the medium term due to our expectation of gradual portfolio expansion, conservative investment policies, and appropriate dividend policy. At the end of September 2021, the company’s net capital ratio (NCR) stood at 53.6%, well above the minimum regulatory requirement of 7%.

We also expect its earnings capacity to remain low over the next few years with a ratio of earnings before taxes to risk-weighted assets (EBT/RWAs) of around 1%. TSFC’s ability to improve profit is restricted by its SFC status which makes it unsuited for aggressive competition and business expansion.

Nonetheless, well-controlled funding costs and operating expenses should help the company maintain profitability over the medium term. For 9M21, the company's ratio of operating expenses to total income was 36.3%, a decrease from 47.1% in 9M20 due to expanded revenue base.

Strong risk position

The company's strong risk position is supported by its prudent risk management policies, which are closely monitored by the Stock Exchange of Thailand (SET), its major shareholder, through board representatives. To mitigate credit risks, the company maintains prudent risk control policies on credit underwritings, marginable securities grading, and margin maintenance monitoring. Asset quality remains sound with no additional credit losses incurred during 9M21. The company's exposure to market risk is manageable as its investment portfolio remains small and low-risk, consisting mostly of government bonds, aligned with its investment policies. Its investment portfolio represented 4% of the company's total assets at the end of September 2021.

Moderate funding and liquidity profile

We view the company's funding and liquidity profile to be adequate due to an asset-liability maturity mismatch at a manageable level. The company relies on short-term borrowings as its main source of funds, while a certain portion of its uses of funds are of longer maturity. Nonetheless, we have no major concerns over the mismatch, thanks to the ample credit facilities TSFC receives from various financial institutions. The company also plans to increase the proportion of long-term borrowings in an effort to address the issue. At the end of September 2021, the company had credit facilities totaling THB8.2 billion, an increase from around THB7 billion at the end of September 2020. About 70% of the credit lines remained undrawn.

BASE-CASE ASSUMPTIONS

TRIS Rating's base-case assumptions for TSFC's operations in 2021-2024 are as follows:

- Total loan portfolio to be around THB5-THB6 billion
- Interest spread to hover around 3%
- Ratio of operating expenses to total income to maintain at approximately 40%

RATING OUTLOOK

The "stable" outlook reflects our expectation that the company will maintain its strong capital position and earnings capability as well as its funding and liquidity profile.

RATING SENSITIVITIES

TSFC's credit upside would materialize if the company were able to meaningfully diversify its revenue mix or exhibit stronger capital and earnings capability for a sustained period. On the contrary, the rating and/or outlook could be revised downward if asset quality weakened significantly or capital, leverage and earnings deteriorated materially with RAC falling below 15% for an extended period.

COMPANY OVERVIEW

TSFC was founded in September 1996. The MOF recognized the need to set up specialized firms to conduct securities-related financing as part of its efforts to develop the Thai capital market. TSFC was founded with initial paid-up capital of Bt1 billion. Its mission was to serve as a reliable source of funds for securities firms. Securities firms needed a reliable source of funds because a regulatory change forced finance companies to separate their finance business from their securities business.

TSFC commenced operations in 1996 by lending its excess funds through the money market. TSFC is the sole company licensed by the MOF to provide securities financing, including margin loan refinancing, loans against pledged securities, and securities repurchase agreements.

TSFC's original shareholders were public and private sector organizations, including the MOF, Government Savings Bank (GSB), Krung Thai Bank (KTB), the Stock Exchange of Thailand (SET), other commercial banks, finance companies, and securities companies. As of June 2007, government-related entities held 26.9% of TSFC's shares, while commercial banks, finance companies, and securities companies held 44.4%. The remaining 28.7% was held by finance and securities companies that were permanently closed as a result of the 1997 financial crisis. This portion came under the management of the Financial Institutions Development Fund (FIDF) after these finance and securities companies were closed by the regulatory authorities. TSFC's board of directors, made up of shareholders' representatives, has contributed the expertise that TSFC needed to develop its policies and business.

In 1997, TSFC introduced other types of loans for securities companies, including margin loan refinancing, loans against pledged securities, and loans made under repurchase agreements. Moreover, the MOF ordered TSFC to launch a special project loan program designed to help cash-strapped securities firms in the early days of the Asian financial crisis.

TSFC's scope of services has expanded. For example, in 2002, TSFC began providing secured securities underwriting for securities companies by issuing a Contingent Agreement to Purchase Letter (CAPL) to underwriters. In 2003, TSFC launched credit balance financing by transferring brokers' margin accounts to its own account. This service provides financial flexibility to securities companies by lowering their net capital reserve (NCR) requirements.

The Thai stock market experienced a remarkable recovery in 2003. As a result, TSFC built up a substantial portfolio of margin loans, launched Employee Stock Option Program (ESOP) financing, as well as loans to investors for private placements (PP), initial public offerings (IPO), and public offerings (PO). IPO and ESOP financings are TSFC's exclusive purview; other securities firms are prohibited from offering these services. TSFC has launched other new products and services, including mutual fund guarantees and securities borrowing and lending (SBL). TSFC is permitted to conduct SBL services, provide securities underwriters with contingent agreements to purchase the unsold portions of securities offerings, and provide guarantees to mutual fund investors.

TSFC was greatly impacted after the Thai stock market plummeted in October 2008. TSFC signed a debt restructuring agreement (DRA) with its major creditors on 20 March 2009. On 22 July 2009, the company was able to fulfil a key condition in the DRA: raising at least Bt1 billion of new equity capital from its existing shareholders, new investors, and through a debt-equity conversion. TSFC obtained Bt1,016.7 million in new equity capital at a par value of Bt10 per share. TSFC registered the new share issues at the Ministry of Commerce on 24 July 2009. The Securities and Exchange Commission (SEC) allowed TSFC to restart its margin loan business on 28 July 2009. After the recapitalization, the SET became TSFC's largest shareholder, holding a 24.66% stake, followed by the MOF (10.56%), KTB (6.02%), and GSB (4.92%).

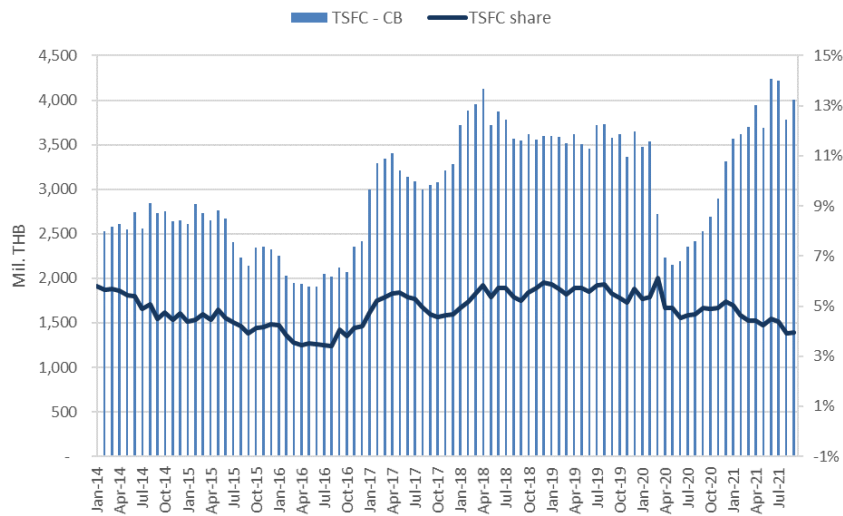
TSFC raised new equity capital in July 2014. After the capital increase, TSFC's equity base was strengthened. On 22 July 2014, TSFC raised Bt532 million through a private placement with its major shareholders, the SET, the MOF, and GSB, resulting in an increase in TSFC's shareholders' equity to Bt1,549 million from Bt1,016 million and making the SET its largest shareholder, owning 40.65%, followed by the MOF (10.56%) and GSB (9.5%). Other shareholders are commercial banks (11.89%), securities companies (10.9%), asset management funds (9.7%), insurance companies (2.82%), and others (0.03%).

In the second half of 2014, TSFC started offering loans to securities companies, a product it used to offer. In 2017, TSFC started offering LBMT and block trade financing as additional product programs to further serve the company's mission to act as a liquidity provider for securities companies. In September 2018, TSFC has received Certificate of Registration Information Security Management System – ISO/IEC 27001:2013 from The British Standards Institution (BSI), which certifies that the company's management of information security applied to the electronic fund transfer operation using BAHTNET complies with the requirements of ISO/IEC 27001:2013.

In December 2019, GSB acquired more stakes in TSFC by purchasing 15,095,418 shares from TSFC's existing shareholders. Together with GSB's previously owned shares in the company, therefore, GSB now holds 29,812,018 shares in TSFC, increasing its stakes to 19.25% in TSFC from 9.50%.

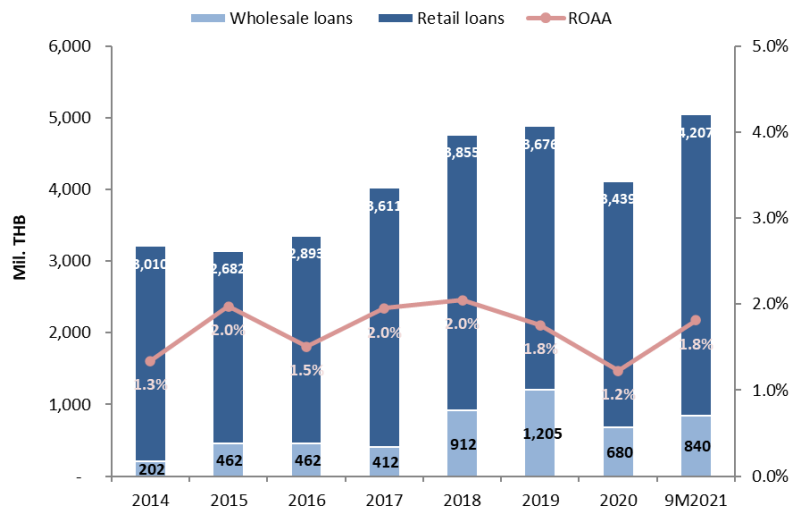
KEY OPERATING PERFORMANCE

Chart 1: TSFC's Margin Loans and Market Share after Recapitalization in 2014



Source: 1) Stock Exchange of Thailand (SET)
2) TSFC
3) TRIS Rating's database

Chart 2: TSFC's Loan Mix and Returns on Average Assets (ROAA)



Source: TSFC

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS

Unit: Mil. THB

	Jan-Sep 2021	Year Ended 31 December			
		2020	2019	2018	2017
Total assets	5,278	4,500	5,030	4,682	4,354
Total loans (ending gross receivables)	5,047	4,119	4,881	4,767	4,023
Allowance for doubtful accounts***	8	8	7	304	320
Short-term borrowings	3,203	2,355	3,152	2,800	2,446
Long-term borrowings	0	0	0	0	0
Shareholders' equity	1,837	1,805	1,794	1,747	1,686
Net interest income	148	165	207	216	196
Provision for bad debt and doubtful accounts**	0	0	(5)	(3)	8
Non-interest income	1	1	1	0	1
Operating expenses	67	93	106	103	98
Earnings before taxes	83	73	107	116	92
Net income	66	58	85	93	74

Unit: %

	Jan-Sep 2021	Year Ended 31 December			
		2020	2019	2018	2017
Profitability					
Net interest and dividend income/average assets	4.05 *	3.45	4.26	4.77	5.21
Fees and services income/average assets	0.01	0.01	0.02	0.01	0.03
Operating expenses/total income	36.28	47.14	38.47	37.15	39.81
Operating profit/average assets	2.26 *	1.54	2.20	2.56	2.44
Earnings before taxes/average risk-weighted assets	1.68 *	0.86	1.22	1.45	1.38
Return on average assets	1.81 *	1.23	1.76	2.05	1.95
Return on average equity	4.87 *	3.25	4.82	5.39	4.43
Asset Quality					
Non-performing loans/total loans	0.14	0.17	0.15	6.31	7.67
Provision for bad debts and doubtful accounts**/average loans	0.00 *	0.00	(0.10)	(0.07)	0.23
Allowance for doubtful accounts***/total loans	0.15	0.18	0.15	6.38	7.96
Capitalization					
Risk-adjusted capital ratio	18.76	22.01	19.57	20.23	22.15
Debt/equity (times)	1.87	1.49	1.80	1.68	1.58
Funding and Liquidity					
Stable funding ratio	86.34	103.24	96.81	99.13	103.60
Liquidity coverage measure (times)	0.06	0.07	0.04	0.06	0.11
Short-term borrowings/total borrowings	100.00	100.00	100.00	100.00	100.00

* Annualized

** Expected credit losses under TFRS 9

*** Allowance for impairment losses under TFRS 9

RELATED CRITERIA

- Nonbank Financial Institution Methodology, 17 February 2020

TSFC Securities PLC (TSFC)

Company Rating:	BBB
Rating Outlook:	Stable

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