

KIATNAKIN PHATRA BANK PLC

No. 60/2024
24 April 2024

FINANCIAL INSTITUTIONS

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

Last Review Date: 25/05/23

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) and the ratings on its senior unsecured debentures at "A", and the ratings on its Basel III Tier 2 subordinated debentures at "BBB+" with a "stable" outlook.

The ratings continue to reflect KKP's increased operating scale in the hire purchase (HP) business, adequate capital, continued strong performance in the capital market business, and moderate funding profile. However, the ratings factor in our concerns over deterioration of its asset quality and lower profitability from a sizeable loss on the sale of repossessed assets. The lack of improvement or further deterioration could pressure its credit profile.

KEY RATING CONSIDERATIONS

Increased operating scale in HP business

KKP's growth in the auto loan portfolio has surpassed that of peers, achieving a compound growth rate (CAGR) of 14.8% in 2020-2023. Total auto loans reached THB187 billion at end-2023. Currently, KKP ranked the fourth among Thai commercial banks in the HP business. The bank leverages its expanded customer base by cross-selling its auto title loan product branded as "Rod Riak Ngern".

Due to economic challenges and the uncertain development of the used car market, KKP intends to take a cautious approach in auto lending, with the auto loan portfolio likely to contract in 2024-2026. This is primarily attributed to asset quality deterioration in both new car and used car segments. Over the next three years, KKP plans to diversify further into the auto title loan segment.

Based on KKP's management guidance, we assume the growth of the bank's auto title loan to range between 15%-25% in 2024-2026. However, outstanding loans for new cars and used cars are expected to contract over the next three years.

Asset quality under pressure

KKP's aggressive expansion in the auto HP segment over the past three years has resulted in deterioration of asset quality, which has become evident since 2022. While the asset quality of its new auto loans booked in 2023 has improved, the non-performing loan (NPL) formation of auto loans booked in 2023 remained noticeably higher than those levels observed in 2018-2019.

The bank's NPL formation rate was at 2.26% in 2023, moderately higher compared with our expectation and historical average of less than 2% in the past. Stage-2 loans also rose to 7.1% of total loans from 5.8% at end-2022.

We expect the bank's NPL ratio to hover above 3% in 2024-2026 given our assumption of a contracting outstanding loan book. This is based on our view of an uneven economic recovery and the potential customer's financial strain resulting from increased interest rates.

While we expect KKP to be able to manage its asset quality as it tightens underwriting standards, we remain concerned over the losses on the sale of repossessed cars. These losses significantly exceeded our expectation, surging by 164% compared with 2022. This resulted from the plummeting used car prices due to a combination of (i) an influx of used car supply in the market given the larger number of repossessed cars; and (ii) the slower sale of used

cars as price competition from electric cars intensifies and lenders tighten underwriting standards.

As a result of weakening asset quality and the surge in loss on sales of repossessed cars, KKP's credit cost were above our expectation, rising to 2.8% in 2023 from 2.0% in 2022. Nonetheless, our "stable" outlook on KKP is premised on our expectation that the bank's asset quality and losses on sale of repossessed cars will gradually recover from 2024 onwards. We project KKP's credit cost (including losses on the sale of repossessed cars) to range between 2.2%-2.7% over the next three years. Further deterioration beyond our base-case scenario could negatively impact the ratings.

Waning earnings capacity, likely to improve gradually

KKP's financial performance in 2023 was below our expectation. While the bank's total operating income was in-line with our projection, a notable surge in provisioning expenses led to a 28% year-on-year (y-o-y) drop in net profit to THB5.5 billion. KKP's return on average assets (ROAA) stood at 1.0% in 2023, a decline from 1.6% in 2022.

With our base-case scenario that earnings are likely to recover slowly over the next three years, we expect KKP's ROAA to stay relatively flat in 2024 and gradually recover in 2025-2026 but remain below its five-year historical average of around 1.5%. This will be supported by lower credit costs and an expansion in net interest margin (NIM) as the bank diversifies to higher-yielding products while funding costs will likely decline. We project its NIM to remain in the 4% range.

Adequate capital position

We expect KKP to maintain its adequate capital position over the next three years, considering its selective growth strategy over the coming years. KKP's consolidated common equity tier-1 (CET-1) ratio was at 13.3% at end-2023, relatively stable compared with the level at end-2022. We project KKP's CET-1 ratio to increase marginally in 2024-2026, assuming loan growth of 2% in 2024, and gradually ramp up to a mid-single-digit growth by 2026. We also assume the dividend payout ratio of 75% over the next three years.

We view that KKP has a well-prepared capital management plan in place, which could support its capital position. The bank has outstanding warrants which, if exercised, could result in a potential capital increase of about THB9 billion. However, we have not factored in the exercise of warrants in our base case scenario.

Moderate funding profile

KKP's funding profile is assessed as moderate. The proportion of retail deposits to total deposits was 76.6% at the end of 2023. We see good progress in improving its deposit franchise over the past three years with the introduction of new deposit products, including e-saving accounts and foreign currency deposit (FCD) accounts, "KKP Smart Settlement" or KKPSS, a deposit account for the settlement of investment transactions. KKPSS has helped the bank reduce the gap in deposit costs compared with the industry average.

The balance of KKPSS dropped significantly to THB55 billion from THB80 billion at end-2022. The change was largely due to a shift towards the bank's own term deposit accounts and the fixed income funds of its own asset management arm, Kiatnakin Phatra Asset Management Co., Ltd. (KKPAM), following policy rate hikes.

At end-2023, the bank's current account and savings account (CASA) deposits to total deposits stood at 36%, decreasing from 59% at end-2022. This decline is in line with other small-sized banks. In terms of deposit costs, the gap between KKP's deposit costs versus industry average has widened marginally to 0.7% in 2023 from 0.5% in 2022.

Sufficient liquidity

In our view, KKP's liquidity position will remain sufficient over the next 12 months. The bank's liquidity coverage ratio (LCR) stood at an average of 126% at the end of the second quarter of 2023, above the regulatory requirement albeit weaker than the average for Thai banks of 188% reported by the Bank of Thailand (BOT). As of end-2023, its liquid assets made up 21% of total assets.

BASE-CASE ASSUMPTIONS

The following are our base-case assumptions for KKP in 2024-2026:

- Loan growth: 2%-7% per annum
- Net interest margin: 4.3%-4.4%
- Cost-to-income: 40%
- Credit cost: 2.2%-2.7%
- NPL ratio (excluding purchased or originated credit impaired (POCI) and interbank assets): 3.3%
- NPL formation rate: 1.8%-2.2%
- CET-1 ratio: 13.5%-13.6%

RATING OUTLOOK

The “stable” outlook reflects our expectation that KKP will maintain asset quality and earnings capacity at acceptable levels while ensuring adequate capital position. At the same time, we expect healthy financial performance and revenue diversification to be sustained by the bank’s synergies with its capital market and wealth management units.

RATING SENSITIVITIES

The ratings and/or outlook could be revised upward if KKP strengthens its capital position significantly, with the CET-1 ratio staying well above 15% for a sustained period, while continuing to improve its asset quality and earnings capacity as well as commercial banking franchise. We could revise the outlook and ratings downward if its asset quality and/or earnings capacity weakens below our base-case scenario or CET-1 ratio falls below 12%.

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 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 19 April 2024)

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 Securities Co., Ltd. (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 in KKP CAPITAL, while KKP CAPITAL held shares of Kiatnakin Phatra Securities PLC (KKPS) and KKPAM. KKP Tower Co., Ltd. (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 a new subsidiary under the name “KKP Dime Co., Ltd.”. KKP Dime’s main objectives are to provide financial and investment services through digital channels. Kiatnakin Phatra Financial Group through KKP Capital PLC holds 100% of the total shares of KKP Dime.

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS¹

Unit: Mil. THB

	-----Year Ended 31 December -----				
	2023	2022	2021	2020	2019
Total assets	545,327	507,637	436,123	363,411	311,690
Average assets	526,482	471,880	399,767	337,551	309,010
Interbank and money market items	62,029	45,732	55,238	32,771	11,982
Investments	52,297	50,551	39,205	34,603	39,201
Loans and receivables	405,493	383,839	315,653	271,951	238,267
Loan loss reserves	20,787	18,327	16,620	13,234	10,589
Deposits	358,903	331,464	288,382	251,526	172,174
Borrowings ²	93,268	85,086	62,169	39,504	76,253
Shareholders' equities	61,253	58,111	51,162	46,626	44,011
Average equities	59,682	54,637	48,894	45,318	43,176
Net interest income	22,294	19,081	15,701	14,679	12,316
Net fees and service income	5,476	6,165	6,074	4,336	4,604
Non-interest income ³	6,534	8,760	9,131	6,969	7,436
Total revenue	28,828	27,842	24,831	21,648	19,752
Operating expenses ⁴	11,088	11,472	9,745	9,758	9,355
Pre-provision operating profit (PPOP)	17,740	16,369	15,087	11,890	10,397
Expected credit loss	10,953	6,880	7,290	5,404	3,099
Net income	5,456	7,616	6,355	5,143	5,990

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 -----				
	2023	2022	2021	2020	2019
Earnings					
Return on average assets	1.04	1.61	1.59	1.52	1.94
Net interest margins	4.52	4.36	4.28	4.73	4.28
Risk-adjusted net interest margins	2.30	2.79	2.29	2.99	3.20
Net interest income/average assets	4.23	4.04	3.93	4.35	3.99
Non-interest income ⁵ /average assets	1.24	1.86	2.28	2.06	2.41
Net fees and service income/total revenue	19.00	22.14	24.46	20.03	23.31
Cost-to-income	40.41	41.07	39.00	41.16	46.73
Capitalization					
CET-1 ratio	13.31	13.32	13.62	14.33	13.61
Total capital ratio	16.61	16.63	17.35	18.28	17.20
CET-1/total capital	80.10	80.11	78.48	78.38	79.12
Asset Quality					
Credit costs	2.82	2.01	2.55	2.15	1.33
Non-performing loans/total loans ⁶	3.17	3.28	3.09	2.93	4.03
Loan loss reserves/non-performing loans ⁶	164.58	148.25	174.98	170.74	110.77
Funding & Liquidity					
CASA/total deposit ⁷	35.75	59.15	59.06	52.49	37.54
Loan/total deposits ⁷	110.89	113.87	106.42	105.27	137.73
Deposits ⁸ /total liabilities	74.14	73.74	74.91	79.40	64.32
Liquidity coverage ratio	N.A.	131	147	141	119
Liquid assets/total assets	21.22	19.16	21.94	18.95	16.78
Liquid assets/total deposits ⁸	30.29	27.67	31.37	26.30	27.59

5 Net of fee and service expenses

6 Based on reported NPL, excluding accrued interests and interbank assets

7 Excluding bills of exchange and interbank borrowing

8 Including bills of exchange and interbank borrowing

N.A. Not available

RELATED CRITERIA

- Financial Institution Rating Methodology, 24 November 2023
- Bank Hybrid Capital Rating Methodology, 24 December 2021

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+
KKP338A: THB3,000 million Basel III Tier 2 capital securities due 2033	BBB+
KKP240A: THB2,300 million senior unsecured debentures due 2024	A
KKP240B: THB5,300 million senior unsecured debentures due 2024	A
KKP24NA: THB5,000 million senior unsecured debentures due 2024	A
KKP251A: THB3,000 million senior unsecured debentures due 2025	A
Rating Outlook:	Stable

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