

BUALUANG SECURITIES PLC

No. 213/2020
22 December 2020

FINANCIAL INSTITUTIONS

Company Rating: AA
Outlook: Stable

Last Review Date: 27/12/19

Company Rating History:

Date	Rating	Outlook/Alert
21/12/17	AA	Stable
19/09/12	AA-	Stable
18/11/11	A-	Positive
27/05/10	A-	Stable

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RATIONALE

TRIS Rating affirms the company rating on Bualuang Securities PCL (BLS) at “AA” with a “stable” outlook. BLS’s rating is enhanced from its stand-alone credit profile to reflect its status as a highly strategic subsidiary of Bangkok Bank PCL (BBL, rated “BBB+/Stable” by S&P Global Ratings). The company’s stand-alone rating also takes into consideration its strong market position in the securities business, solid capital and earnings assessment, prudent risk management policies, and strong funding and liquidity profile.

KEY RATING CONSIDERATIONS

A highly strategic subsidiary of BBL

We view BLS as a highly strategic subsidiary of BBL as the company serves as a capital market arm of BBL providing a comprehensive range of capital market solutions for BBL’s clients. BLS is wholly owned by BBL. Business referrals between the two entities have been part of the group’s strategy. Currently, approximately 50% of the company’s newly added client accounts were referred from BBL. In addition to business support, BLS has also received financial supports from BBL in the form of credit lines that help enhance the company’s funding profile. We are of the view that it is highly likely that the linkage between BBL and BLS will be maintained in the foreseeable future.

Strength in business stability

We expect BLS to maintain strong business stability over the long term. Its competitive strengths are underpinned by its comprehensive and value-added products and services that help the company differentiate itself from competitors and enable it to continuously expand its client base. We expect the company to continuously strengthen and broaden its product and service offerings in response to constantly changing investor demand. New services recently introduced include Global Investing, which gives its clients direct access to offshore investments.

As for its core businesses, the company holds leading market shares across a broad range of business lines. For the first six months of 2020 (1H2020), the company’s securities brokerage revenue share ranked first among peers with a share of 8.4%. Its derivatives brokerage revenue share ranked third among peers with a share of 7.5% for the same period. The company’s revenue share in investment banking business also ranked among the top with a share of 13% based on a 3-year average (2017-2019).

Strong fee-based revenue

The company has well-balanced revenue sources with a high contribution from fee-based income and healthy brokerage commission. In 2019, brokerage revenue, fees and service income, and trading gains contributed 48%, 23%, and 11% of total revenue, respectively, compared with the industry average of 52%, 17%, and 12%.

The company’s solid franchise in securities brokerage and investment banking also helps sustain its financial performance. This was evident in 1H2020 where the strong revenues from these businesses made up for the large losses incurred by the derivative warrants (DW) business due to excessive market volatility. As a result, BLS was able to report relatively stable net income of THB324 million for 1H2020, compared with THB330 million for 1H2019.

We view that the company has relatively low client revenue concentration, thanks to its extensive and expanding client base, especially its retail clients with a total of over 400,000 accounts at the end of September 2020. Brokerage fees from the top-20 clients also accounted for only 13% of the company's total securities brokerage fees for 9M2020.

Solid capital profile

A notable credit factor that has underpinned BLS's rating is its solid capital profile as measured by the risk-adjusted capital ratio (RAC). We expect the company's RAC to sustain at approximately 36% on average over the 5-year period (2018-2022), thanks to its robust equity base and moderate investment in high-risk assets. At the end of June 2020, the company's shareholders' equity remained one of the highest in the industry at THB8.8 billion. With its conservative dividend policy and cautious business expansion plans, we believe the company's capital and leverage will remain strong over the medium term. The company also ended 2019 with a net capital ratio (NCR) of 160.6%, well above peers and the regulatory requirement of 7%.

The company's capital strength is supported by its strong earnings capacity. We expect that the company will be able to maintain its revenue-generating capabilities across all business lines while keeping operating costs under control and sustain healthy earnings over the next few years. We estimate its earnings before taxes to risk-weighted assets (EBT/RWAs) will hover around 5% over the medium term despite losses from DWs during the first half of 2020. The company has taken steps to enhance its risk control policies to mitigate losses from excessive volatility. For 1H2020, the company's annualized EBT/RWAs was 2.6%, compared with 3.5% in 1H2019.

We also expect that the company will continue to maintain relatively low operating costs by closing down some branches and maximizing utilization of existing branches. For 1H2020, the company's ratio of operating expenses to net revenue was 56.0%, lower than the industry average of 64.5%.

Prudent risk management policies

The company's prudent risk management policies and low risk appetite underpin its risk position. The level of risk exposure associated with its products has generally been under control, in our view. Following the losses from its DW business due to an unexpectedly volatile stock market during the first half of 2020, the company promptly scaled back its DW business and tightened its risk management policies to prevent such losses from recurring in the future. The company generally does not engage in speculative trading activities, which helps limit market risk.

The company has maintained its conservative credit risk control policies, with prudent credit extensions and strict margin call enforcements for both equity margin lending and derivatives trading. As a result, the company did not incur any credit losses during the first six months of 2020 despite the severe stock market plunge in March 2020.

Strong funding and liquidity profile

The company's strong funding profile is supported by its sound equity base. We expect the company's stable funding, as measured by the gross stable funding ratio (GSFR) to remain high at approximately 300% over the next few years.

The company's strong liquidity position is indicated by the assessed liquidity coverage metric (LCM) of around 6 times based on a 5-year average (2018-2022). Readily available credit facilities from various financial institutions, with the majority of the facilities from BBL, also help enhance its financial flexibilities. At the end of September 2020, the company had available credit facilities of around THB28 billion.

BASE-CASE ASSUMPTIONS

TRIS Rating's base-case assumptions for 2020-2023:

- Market share in securities trading value to be around 4%-5%.
- Average commission rate to be maintained at approximately 15 basis points (bps).
- Ratio of operating expenses to net revenue to hover around 50%.

RATING OUTLOOK

The "stable" outlook reflects the expectation that BLS will maintain its status as a highly strategic subsidiary of BBL and continue to receive strong support from its parent bank.

RATING SENSITIVITIES

The rating and/or outlook of BLS could be revised upward or downward, should there be any changes in BBL's credit profile or if TRIS Rating perceives any significant changes in the degree of support BLS receives from BBL or if there are any changes to BLS's group status as a highly strategic subsidiary of BBL.

COMPANY OVERVIEW

BLS was established by Bualuang Finance Co., Ltd. after it acquired the securities brokerage license of BOA Securities Co., Ltd. from BOA Finance Co., Ltd. in 2001. BLS's initial paid-up capital was THB100 million.

In December 2001, BLS strengthened its competitive position in the securities business by acquiring the retail brokerage business of JP Morgan Securities (Thailand) Ltd., formerly known as JF Thanakom Securities Co., Ltd. At the time of the acquisition, JP Morgan was one of the top three securities firms. BLS bought the related assets, and the staff of JP Morgan securities became employees of BLS. As a result of a capital injection by Bualuang Finance and JP Morgan, BLS's paid-up capital increased from THB160 million to THB200 million.

In 2002, BLS acquired JP Morgan's private fund management business. BLS was authorized by the Securities and Exchange Commission (SEC) to operate other securities-related businesses including private fund management, financial advisory services, and act as a selling agent. An additional private placement offering to existing shareholders (mainly BBL and JP Morgan) raised BLS's paid-up capital to THB250 million at the end of 2002. During the last quarter of the same year, BLS began offering Internet trading services to its clients.

In 2004, BLS lowered its par value to THB2 per share from THB10 and offered seven million new shares to directors and employees. In November of the same year, the company issued THB300 million in convertible debentures to BBL. The debentures could be converted into 20.5 million shares when exercised. At the end of 2004, paid-up capital stood at THB264 million.

The company was listed on the Stock Exchange of Thailand (SET) in February 2005 by offering 40 million shares, comprising 27.5 million new shares and 12.5 million shares from existing shareholders, at THB12 per share. The proceeds from the initial public offering (IPO) and the conversion of BBL's convertible debentures raised paid-up capital to THB360 million at the end of 2005. BBL's shareholding in BLS was reduced from 61.29% to 56.34% after the IPO.

To improve the quality of research and staff capabilities as well as to expand the securities brokerage business to markets abroad, BLS signed a Research Support Agreement with a company in the Morgan Stanley Group in 2006. This contract was later converted to an Exclusive Partner Agreement in 2007. Overseas trading volume improved substantially as a result of this strategic partnership, leaping from THB23 billion in 2005 (9% of BLS's total trading volume) to as high as THB100 billion in 2007 (32% of total volume). Apart from the constant flow of brokerage business and the research collaboration, BLS benefits from the occasional opportunity to co-host overseas road shows with Morgan Stanley.

BLS established a business referral program with BBL and signed an Introducing Agent Agreement in 2007. The aims of the agreement are to expand BLS's retail customer base and utilize the network of its parent company more efficiently. This arrangement did not work well in the beginning, but after years of adaptation, it has started to pay off.

In 2011, BLS paid a stock dividend to its shareholders at a ratio of one new share for every two existing shares. The stock dividend allowed BLS to reclassify THB180 million in retained earnings as paid-up capital. As a result, BLS's paid-up capital increased to THB540 million at the end of 2011, rising from THB360 million a year earlier.

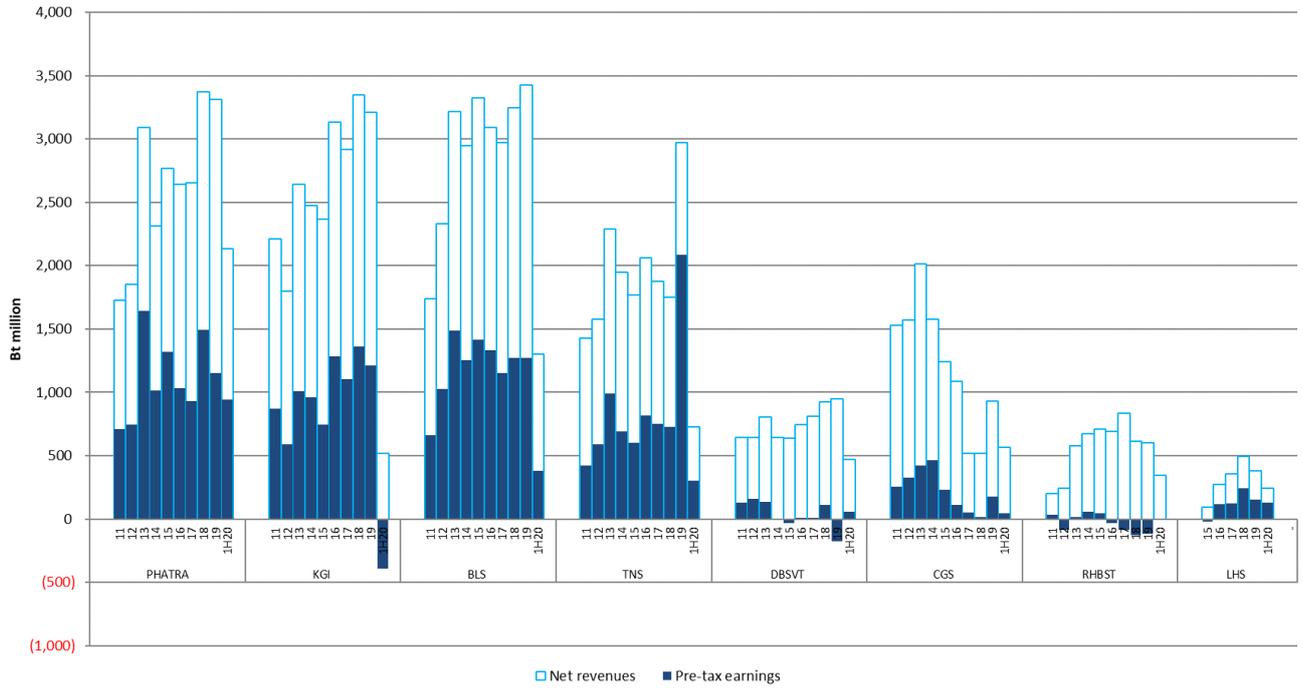
In November 2011, BLS received a letter of intent from BBL. BBL intended to make a tender offer to purchase all of BLS's shares, subject to certain conditions. After those conditions were fulfilled, the tender offer was announced by BBL on 17 January 2012. The tender offer period covered 45 business days, starting from 18 January 2012, at a tender offer price of THB22 per share. After the tender offer, BBL's shareholding in BLS reached 99.70%. BLS's shares were formally delisted from the SET on 7 April 2012.

BLS raised THB1.6 billion in new equity capital in November 2013. BLS intends to use the new capital to expand its underwriting capacity, margin loan portfolio, and DW business.

In mid-2014, BLS set up a new subsidiary, Bangkok Capital Asset Management (BCAP). BLS created BCAP in order to separate its asset management business from the securities business. BCAP started operations in January 2015. All the private funds and provident funds managed by BLS will be transferred to BCAP.

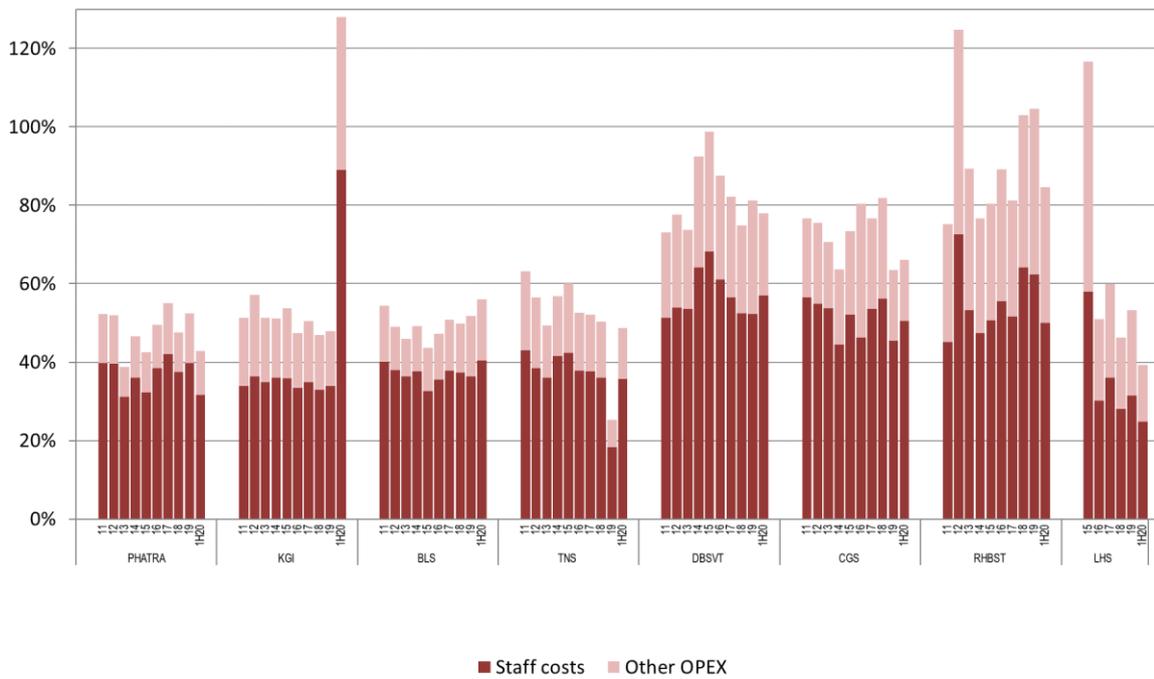
KEY OPERATING PERFORMANCE

Chart 1: Net Revenues and Pre-tax Earnings of Selected Brokers in 2011-1H2020



Sources: Financial statements of each company

Chart 2: Staff Cost and Other Operating Expenses of Selected Brokers in 2011-1H2020 (% of Net Revenues)



Sources: Financial statements of each company

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS
Unit: Mil. THB

	Jan-Jun 2020	-----Year Ended 31 December -----			
		2019	2018	2017	2016
Total assets	15,255	13,889	14,738	16,203	14,192
Net Investment in securities	7,639	7,613	7,181	7,089	3,194
Total securities business receivables and accrued interest receivables	5,916	5,329	5,765	8,159	5,965
Allowance for doubtful accounts	127	127	127	127	128
Total debts	16	366	127	226	191
Shareholders' equity	8,792	9,307	9,123	8,650	8,257
Net securities business income	1,053	2,993	2,826	2,638	2,769
Total income	1,389	3,608	3,418	3,125	3,219
Operating expenses	728	1,773	1,616	1,510	1,459
Interest expenses	89	182	172	151	130
Net income	324	1,010	1,017	929	1,072

Unit: %

	Jan-Jun 2020	-----Year Ended 31 December -----			
		2019	2018	2017	2016
Profitability					
Brokerage fees/total revenues	90.3	48.2	61.6	59.2	59.6
Fees and services income/total revenues	30.3	23.5	10.6	14.6	6.9
Gain (loss) from trading/total revenues	(44.1)	10.7	10.5	11.1	18.7
Operating expenses/net revenues	56.0	51.7	49.8	50.8	47.2
Pre-tax margin	29.1	37.1	39.1	38.7	43.2
Return on average assets	4.4 *	7.1	6.6	6.1	8.7
Earning before tax/risk-weighted assets	2.6 *	5.1	4.8	4.4	6.2
Asset Quality					
Classified receivables/gross securities business receivables	1.6	1.8	1.6	1.2	1.7
Allowance for doubtful accounts/gross securities business receivables	2.2	2.4	2.2	1.6	2.1
Credit costs (reversal)	0.0 *	(0.0)	0.0	(0.0)	0.0
Capitalization					
Leverage ratio	57.9	63.4	58.4	50.5	58.1
Risk-adjusted capital	29.1	31.1	39.4	25.9	39.6
Funding and Liquidity					
Gross stable funding ratio	253.3	263.2	357.1	245.8	347.7
Liquidity coverage metric (times)	17.3	7.9	10.9	7.1	8.6

** Annualized*
RELATED CRITERIA

- Securities Company Rating Methodology, 9 April 2020
- Group Rating Methodology, 10 July 2015

Bualuang Securities PLC (BLS)

Company Rating:	AA
Rating Outlook:	Stable

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