

# PHATRA SECURITIES PLC

No. 55/2020  
17 April 2020

## FINANCIAL INSTITUTIONS

**Company Rating:** A  
**Outlook:** Stable

**Last Review Date:** 26/04/19

### Company Rating History:

Date	Rating	Outlook/Alert
26/04/19	A	Stable
26/04/18	A-	Positive
13/06/13	A-	Stable

### Contacts:

Preeyaporn Kosakarn

preeyaporn@trisrating.com

Annop Supachayanont, CFA

annop@trisrating.com

Narumol Charnchanavivat

narumol@trisrating.com



WWW.TRISRATING.COM

## RATIONALE

TRIS Rating affirms the company rating on PHATRA Securities PLC (PHATRA) at “A/Stable”. The rating reflects the company’s status as a core subsidiary of the Kiatnakin Phatra Financial Group (KKP), its solid market position in the securities business and good revenue diversification, adequate capital and earnings capability, limited exposure to credit risk, and sufficient funding and liquidity. The rating is, however, constrained by its exposure to market risks associated with its principal investment activities, which affects the risk profile of the company.

## KEY RATING CONSIDERATIONS

### A core subsidiary of KKP

TRIS Rating assesses PHATRA as a core member of the KKP Group based on PHATRA’s status as the group’s important and reputable arm in the capital market business. PHATRA has consistently achieved satisfactory operating results, generating a meaningful contribution to KKP’s net profit, at 15% in 2019. As a wholly-owned subsidiary of KKP, PHATRA has been receiving both business and financial supports from KKP and has been expanding its client base by leveraging KKP’s client base, especially among high-net-worth clients. KKP has been granting PHATRA a large credit line, which serves as an additional source of funds enhancing PHATRA’s financial flexibility.

### Strong business position

PHATRA’s business position is secured by its well-established market presence across business lines. It has strong and stable revenue share in securities brokerage and a solid franchise in investment banking (IB). For the first six months of 2019, the company maintained its 4<sup>th</sup> rank in the securities business with revenue share of 5.7%. In the IB business, it had the highest revenue share among peers rated by TRIS Rating over the past three years. Its wealth management business has also been steadily expanding, enabling the company to continuously earn recurring fee income. At the end of December 2019, its asset under advisement (AUA) was Bt575 billion, a 21% increase from 2018, and its selling agent fee increased by 14% to Bt552 million in 2019.

### Diversified revenue structure

The company also has a well-diversified revenue mix, resulting from solid revenue generating capacity in each business line. For the first six months of 2019, brokerage fees accounted for 45% of total revenue while fees and service income contributed 33%, compared with the industry average of 54% and 14% respectively. We expect the company’s business diversity to remain strong as the company continuously strengthens its competitive advantage in research capabilities and sales coverage that should help maintain its brokerage fee base. In addition, consistent efforts in expanding product offerings should enable the company to grow its wealth management business, further enhancing its ability to generate fee-based income.

### Adequate capital and strong earning capabilities

TRIS Rating expects the company’s capitalization to remain sufficient to absorb unexpected losses from credit risk, market risk, and operational risk. We estimate its risk-adjusted capital ratio (RAC) to hover around 12% over the next few years. The company’s RAC ratio at the end of 2019 was at 12.2%.

It also ends the year with a net capital ratio or NCR of 28%, higher than the regulatory requirement of 7%.

At the same time, the company's earning capability is expected to remain strong over the next few years. We estimate the company's ratio of earnings before tax to risk-weighted assets (EBT/RWAs) to be around 3% over the next few years, compared with its 5-year average (2018-2022) EBT/RWAs of 2.8% and 3.2% in 2019. We believe that the company will continue to build on its competitive strengths in research, IB and wealth management and leverage the synergies among subsidiaries in the KKP Group to sustain its profitability. In addition, we believe that the company will maintain relatively low operating expenses. For the first six months of 2019, operating expenses to net revenue was 53.0%, lower than the industry average of 72.2%.

#### **Limited exposure to credit and market risk**

We view PHATRA's exposure to credit risk as being limited as the company does not engage in margin lending. The company's exposure to counterparty risk from brokerage services remains under control, in our view.

Its exposure to market risk from proprietary trading activities is manageable as the company pursues low-risk trading strategies (such as arbitrage trading strategy) and has no positions that closely track market directions. We expect that the company will continue to maintain adequate risk management systems that should help prevent it from incurring major losses from its investment portfolios.

#### **Adequate funding and liquidity**

We assess the company to have adequate funding, judging by our estimate of its gross stable funding ratio (GSFR) of approximately 140%-150% over the next few years. The company has a well-matched funding mix relative to its funding needs, with GSFR at 152.6% at the end of 2019.

We also assess the company to have sufficient liquidity over the next 12 months. At the end of January 2020, it has credit facilities from several financial institutions totaling Bt2.5 billion, in addition to the credit line provided by KKP. The total amount of available credit facilities should be sufficient to fund the company's operations and cover any liquidity shortfalls should they arise. We expect the company's liquidity coverage metric (LCM) to remain adequate at around 1.2 times over the next few years. The LCM ratio compares broad liquid assets (cash on hand, securities holdings) to balance sheet liquidity needs (short-term debt obligations). The ratio was at 1.0 times at the end of 2019. LCM of at least 1.0 time is deemed adequate based on our benchmark.

#### **BASE-CASE ASSUMPTIONS**

TRIS Rating's base-case assumptions for 2020-2022 are

- Market share by securities trading value to be around 10%
- Average commission rate to be approximately 5 basis points (bps)
- Ratio of operating expenses to net revenue to stay around 50%-55%

#### **RATING OUTLOOK**

The "stable" outlook reflects our expectation that PHATRA will maintain its status as a core subsidiary of KKP and continue to receive strong supports from its parent bank.

#### **RATING SENSITIVITIES**

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

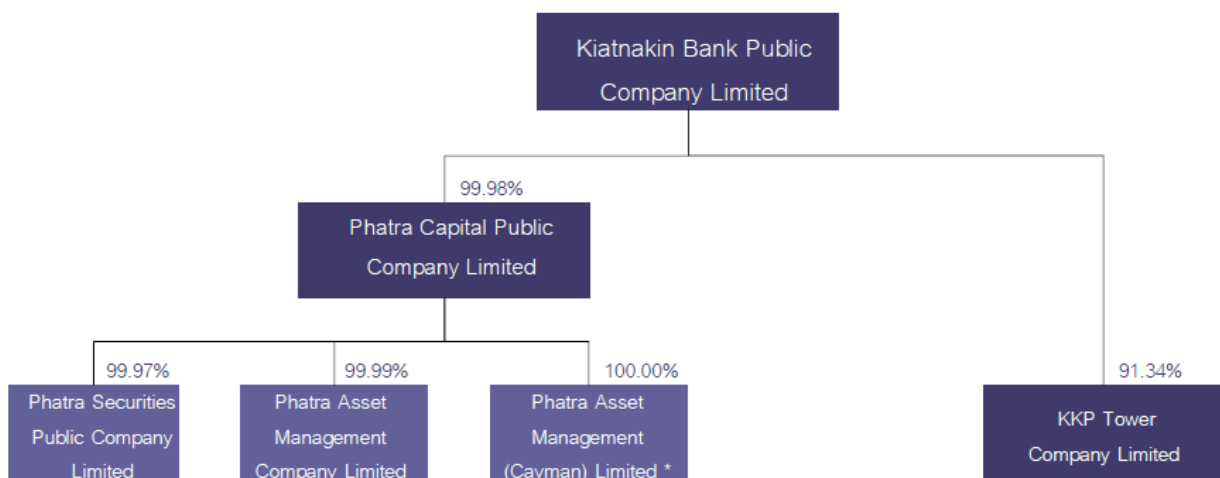
#### **COMPANY OVERVIEW**

PHATRA was spun off from Phatra Thanakit in 1997, becoming a 99.99% owned subsidiary of Phatra Thanakit. Prior to the spin-off, its securities business had been conducted as a department within Phatra Thanakit since 1975. In 1998, PHATRA changed its name to Merrill Lynch Phatra Securities Co. after Merrill Lynch & Co. (ML) and Kasikorn Bank (KBANK) acquired 51% and 49% stakes in PHATRA, respectively. The company changed its name back to Phatra Securities when ML and KBANK sold their combined stakes in Merrill Lynch Phatra Securities to the current management team, employees, and selected investors in 2003. PHATRA became a public company and its shares were listed on the Stock Exchange of Thailand (SET) in 2005.

PHATRA has collaborated with ML since 2003. The alliance covers research, securities brokerage, and investment banking. In 2010, the company restructured. Phatra Capital was set up as a holding company and the Direct Investment (DI) portfolio was transferred from Phatra Securities to the newly set-up Phatra Capital. Phatra Capital was listed on the SET in place of Phatra Securities. The restructuring had three goals: to separate the risks of the agency business and the principal investment business, to give PHATRA more flexibility for future expansion efforts and strategic partnership opportunities, and to minimize conflicts of interest between the agency and principal investment businesses.

As of May 2015, Phatra Capital held a 99.9% stake in Phatra Securities. Before the merger with KKP, PHATRA's expansion efforts were constrained by limitations on capital, size, and business scope inherent in PHATRA's securities business license. The development of, and competition in, the country's and the region's financial markets threatened PHATRA's long-term competitive position. As a result, in April 2012, PHATRA's shareholders approved the merger with KKP at the annual general meeting. In September 2012, the merger was successfully completed. KKP now holds 99.9% of Phatra Capital.

**Chart 1: KKP Group's Structure as of 31 Dec 2019**



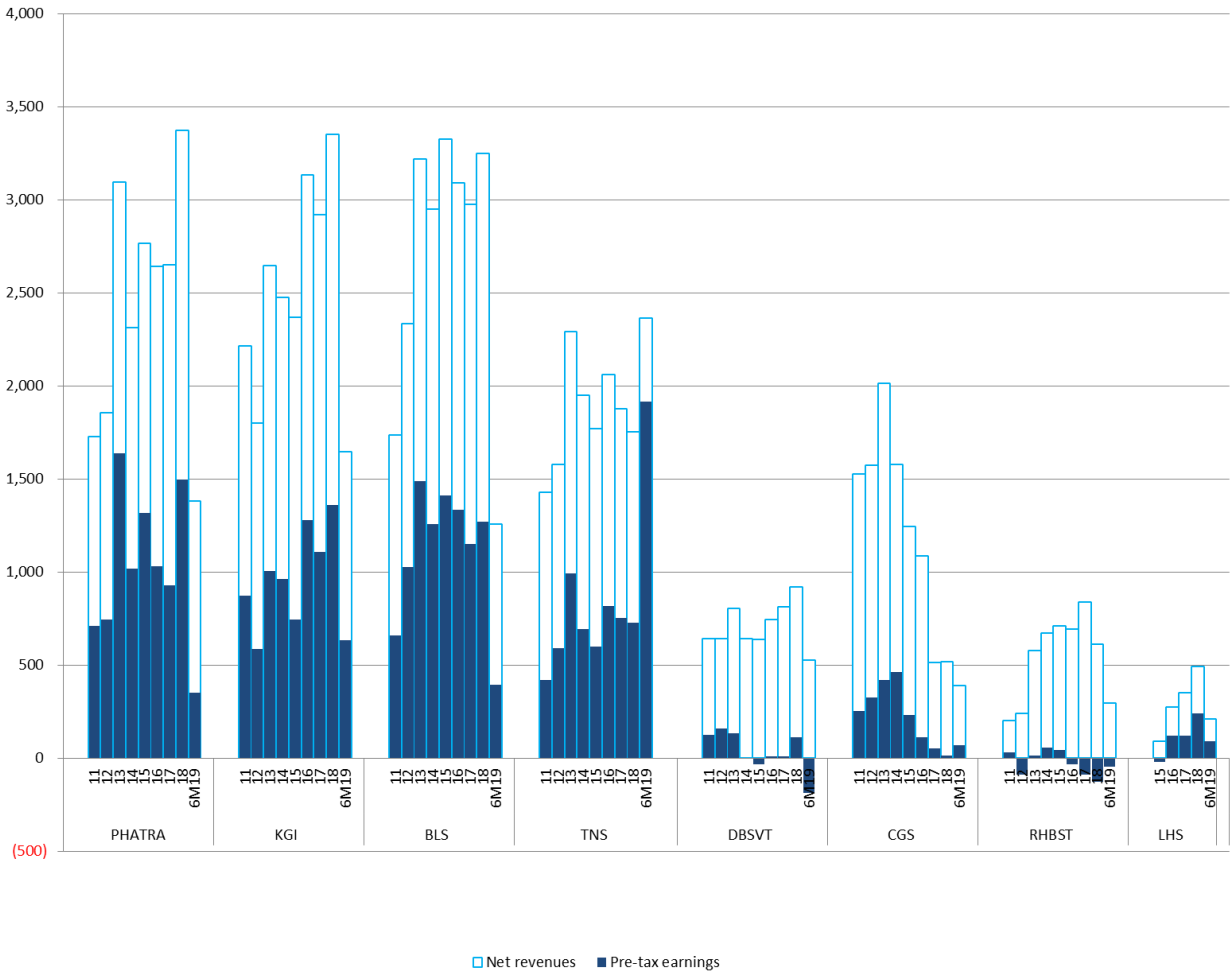
\* As of 1 February 2020, it is in the process of dissolving the company.

In addition, the Bank holds unit trusts in six mutual funds for resolving financial institution problems. The Bank holds 99.95% shares in Asia Recovery 1, 99.59% shares in Asia Recovery Fund 2, 99.97% shares in Asia Recovery Fund 3, 98.91% shares in Thai Restructuring Fund, 95.72% shares in Bangkok Capital Fund and 94.03% shares in Gamma Capital Fund.

Source: PHATRA

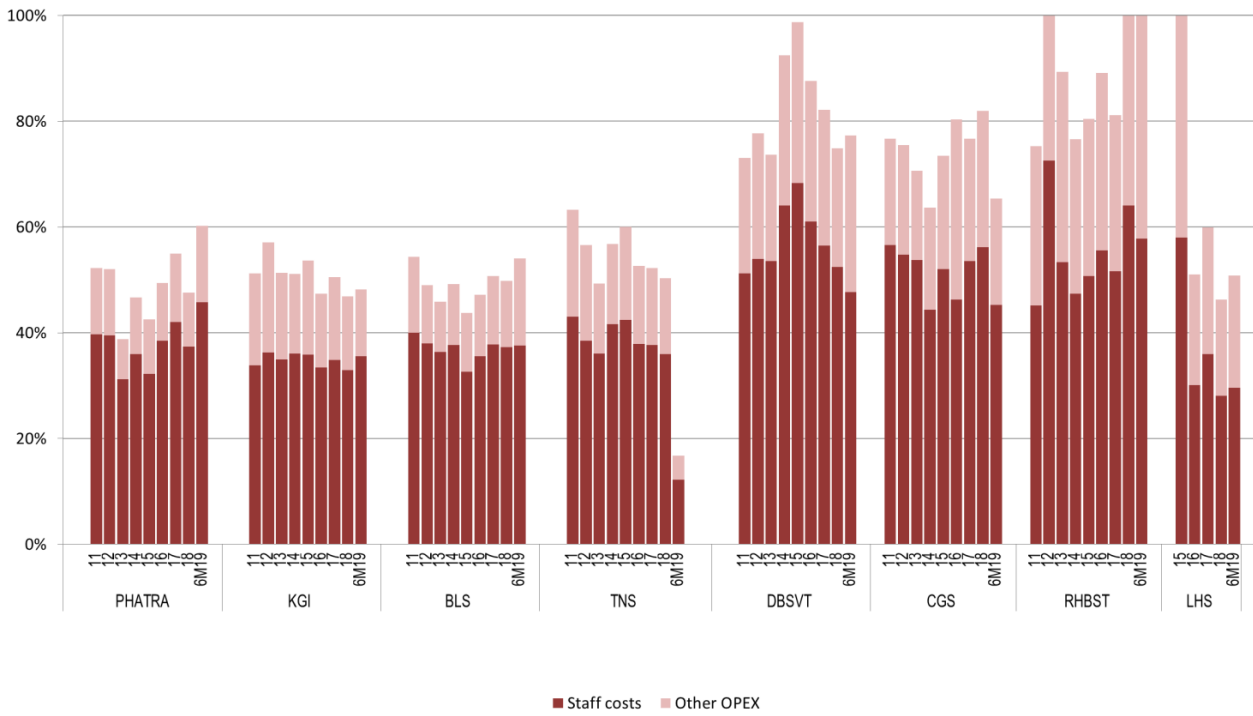
KEY OPERATING PERFORMANCE

Chart 1: Net Revenues and Pre-tax Earnings of Selected Brokers in 2011-1H2019



Sources: Financial statements of each company

**Chart 2: Staff Cost and Other Operating Expenses of Selected Brokers in 2011-1H2019 (% of Net Revenues)**



Sources: Financial statements of each company

**FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS**
*Unit: Bt million*

	-----Year Ended 31 December -----				
	2019	2018	2017	2016	2015
Total assets	20,672	15,957	20,750	21,506	21,122
Net Investment in securities	9,361	5,271	10,727	11,574	4,024
Total securities business receivables and accrued interest receivables	4,620	4,213	4,741	7,593	14,279
Allowance for doubtful accounts	-	-	-	-	-
Total debts	8,949	3,058	8,154	6,978	3,330
Shareholders' equity	5,312	6,100	5,653	5,799	6,007
Net securities business income	2,744	2,971	2,312	2,256	2,409
Total income	3,390	3,549	2,803	2,748	2,850
Operating expenses	1,756	1,604	1,459	1,306	1,176
Interest expenses	77	177	151	108	82
Net income	926	1,197	738	828	1,052

*Unit: %*

	-----Year Ended 31 December -----				
	2019	2018	2017	2016	2015
<b>Profitability</b>					
Brokerage fees/total revenues	40.7	36.3	45.7	49.3	47.8
Fees and services income/total revenues	32.0	31.1	31.5	18.2	10.1
Gain (loss) from trading/total revenues	9.7	10.7	5.6	18.9	28.3
Operating expenses/net revenues	53.0	47.6	55.0	49.5	42.5
Pre-tax margin	34.8	44.4	35.1	39.1	47.7
Return on average assets	5.1	6.5	3.5	3.9	5.6
Earning before tax/risk-weighted assets	3.2	5.0	2.1	2.0	3.2
<b>Asset Quality</b>					
Classified receivables/gross securities business receivables	0.0	0.0	0.0	0.0	0.0
Allowance for doubtful accounts/gross securities business receivables	0.0	0.0	0.0	0.0	0.0
Credit costs (reversal)	0.0	0.0	0.0	0.0	0.0
<b>Capitalization</b>					
Leverage ratio	21.2	30.8	23.7	27.0	28.4
Risk-adjusted capital	12.1	16.6	11.3	11.0	14.5
<b>Funding and Liquidity</b>					
Gross stable funding ratio	152.6	213.4	141.9	130.5	176.8
Liquidity coverage metric	1.0	1.7	0.9	1.2	0.9

**RELATED CRITERIA**

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

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**Phatra Securities PLC (PHATRA)**

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<b>Company Rating:</b>	A
<b>Rating Outlook:</b>	Stable

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**TRIS Rating Co., Ltd.**

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

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