

POLICE GENERAL HOSPITAL SAVING AND CREDIT COOPERATIVE LTD.

No. 141/2018

27 September 2018

FINANCIAL INSTITUTIONS

Company Rating: BBB+

Outlook: Stable

Company Rating History:

Date	Rating	Outlook/Alert
27/07/12	BBB+	Stable

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RATIONALE

TRIS Rating affirms the company rating on Police General Hospital Saving and Credit Cooperative Ltd. (PHSC) at “BBB+”. The rating reflects the status of PHSC as a captive financial service provider for PHSC’s members who work at the Police General Hospital (PGH) and related entities. The rating is also supported by the strong credit profile of PGH as a government entity, its good quality outstanding loans, and the capability of its management team to deliver satisfactory financial performances. The regulatory privileges extended to savings cooperatives also secure loan quality and enhance the competitive edge of PHSC over traditional financial institutions.

However, PHSC’s credit strengths are partially offset by its aggressive funding policy which still relies heavily on deposits from affiliate members. The key-person dependency risk has improved but still exists with the development and implementation of standard operating policies and procedures. The weak capitalization compared with other long-established savings cooperatives has pressures on the rating. The recent and planned regulatory changes will constrain the operating and financial performance of PHSC but in turn will strengthen the operations and control the risk exposure for the cooperative in the long term. However, the regulatory change which reduces the privileges currently enjoyed by savings cooperatives will also put a pressure on the rating.

KEY RATING CONSIDERATIONS

Regulatory privileges enhance competitive edges

TRIS Rating expects the regulatory privileges will continue amidst the current changing legal framework of savings cooperative. Special legal privileges give savings cooperatives some advantages over traditional financial institutions. Savings cooperative and its members are exempt from all major taxes. The high credit quality of loans granted to PHSC’s ordinary members, as is the traditional practice of savings cooperatives, is due to PHSC’s practice of providing loans to ordinary members through agreements with their employers. Loan repayments can be deducted from ordinary members’ monthly payrolls. According to cooperative laws, PHSC has the first-priority claim over any other creditors, except for circumstances under specific legal obligations. This legal support reduces the credit risk of PHSC’s loans to its members and sustains the cash inflows from loan repayments to the cooperative.

TRIS Rating holds the view that the recent and planned regulatory changes are positive factors for the overall savings cooperative industry. Regulatory changes will mandate better risk monitoring and controlling measures, which will in turn strengthen the operations and financial profiles of the savings cooperatives.

The regulatory changes may also constrain the opportunities for growth and result in weaker financial performance in the near term. Rapid growth and high profits are not the main objectives of the savings cooperatives. However, any regulatory changes that reduce the privileges that the savings cooperatives currently enjoy, such as tax benefits and priorities of claims on member’s monthly income, will negatively impact the rating on PHSC.

Strong employment entity

The strong credit profile of PGH, together with the job security of its ordinary

members as employees of a government entity, have ensured the stability of the number of ordinary members and monthly income which consequently secure the ability of debt repayment. This stability continuously increases PHSC's capital base through the monthly obligation of ordinary members to purchase PHSC's shares.

Heavy reliance on external funding

TRIS Rating expects PHSC's funding base will rely on external funding from affiliate members in the long term. The employees of the PGH and its related entities are the only people who are qualified to be ordinary members of PHSC. This type of membership criterion is a normal requirement of traditional savings cooperatives. PHSC also has affiliate members, as other savings cooperatives do. By offering all members attractive interest rates and tax-exempt interest income, PHSC has been able to raise a substantial amount of funds through savings deposits made by affiliate members.

Of the total of members' deposits as of June 2018, approximately 90% were from affiliate members and 10% were from ordinary members. According to the changed regulation, PHSC has continuously reduced its deposits from other savings cooperatives. PHSC's liquidity risk depends on the roll-over rate of the deposit base that has no relationship with either PHSC or PGH and has no other benefits besides attractive interest rates on deposits. Thus, PHSC remained exposed to liquidity risk to a certain extent. PHSC has mitigated this risk by maintaining an adequate portion of liquid assets and unused credit facilities with traditional financial institutions. TRIS Rating expects that as long as PHSC is able to gain tax privileges to offer attractive interest rates, coupled with a conservative investment policy to maintain a relatively high portion of liquid assets, the level of liquidity risks is acceptable.

Good quality loans

According to the current savings cooperative's legal framework, TRIS Rating expects PHSC will have good quality loans. PHSC has expanded the amount of loans made to other savings cooperatives since fiscal year 2010 (FY2010). These loans are expected to yield returns higher than the returns from the investment portfolio. As of late, demand for loans from ordinary members remained quite small, due to the relatively high profiles of its ordinary members and PHSC's underwriting criteria to control the risk exposure to each member.

PHSC's loan portfolio accounted for 52%-57% of total assets during FY2013-FY2017, increasing from 44% during FY2010-FY2012. At the end of June 2018, 94% of the loan portfolio was loans made to other savings cooperatives while the remainders were loans made to ordinary members. PHSC has been able to mitigate its loan concentration risk involving lending to other cooperatives by expanding its borrower base. The loan made to the 10 largest cooperatives constituted 33% of total borrowing as of June 2018, reducing from more than 50% in 2015. The recent new release of single lending limit regulation will reduce the loan concentration risk. PHSC has had no non-performing loans (NPLs) (overdue more than 90 days) since FY2007, whether it was lending to other savings cooperatives or to ordinary members.

Weak capitalization

PHSC's capitalization is considered weak due to its aggressive funding policy. Although the paid-up share capital increased continuously, the aggressive expansion of the deposit base which came mostly from deposits by affiliate members has still put the pressure on the ratio of PHSC's equity to total assets. Although the ratio of PHSC's equity to total assets rose to 10.4% at the end of June 2018 after PHSC reduced the deposit from other cooperatives, the level was considered low when compared with the ratio of around 40% of other long-established large savings cooperatives. With a funding policy that emphasizes deposits, PHSC's capitalization is expected to stay at this low level for a long time.

Key-person risk reduces but still exists

PHSC has been able to pay dividends to shareholders at the maximum level allowed by law at 10% of paid-up shares, since FY2009. PHSC's financial position and performance are dependent on a key member of the management team. PHSC has been developing and implementing standard operating policies and procedures, as well as obtaining various support tools to cover all of its main business activities. This will help mitigate the risk of an over reliance on one person.

RATING OUTLOOK

The "stable" outlook reflects the expectation that PHSC will be able to maintain its deposit base and deliver a performance which will deliver satisfactory returns to its ordinary members.

RATING SENSITIVITIES

The possibilities for credit upsides are limited based on the existing institutional framework of savings cooperatives. On the contrary, more aggressive operating and financial policies of PHSC or any regulatory changes that reduce privileges for savings cooperatives might impact the rating.

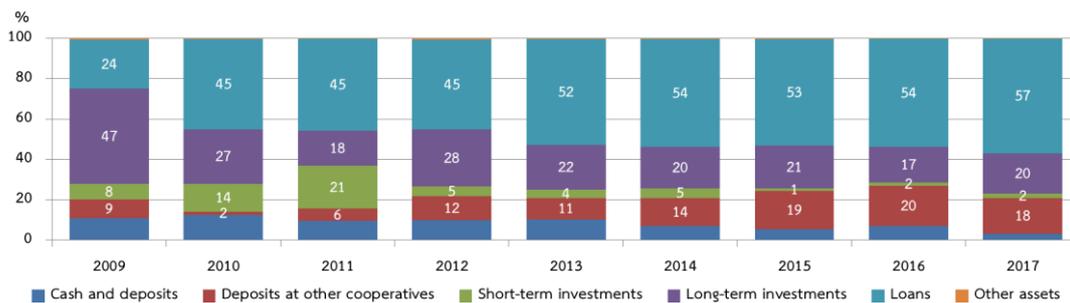
COMPANY OVERVIEW

PHSC was established in 2002 with the initiative of the top management team of the PGH. Before establishing PHSC, the hospital staff who wanted the benefits and services of a savings cooperative had to be members of the Saving and Credit Cooperative of Royal Thai Police Headquarters Ltd. To enlarge its funding base, PHSC started to accept affiliate members who were allowed to use only the deposit service.

At the end of June 2018, PHSC had 1,621 ordinary members and 3,089 affiliate members. PHSC’s total assets were Bt18,840 million at the end of FY2017. PHSC is classified as a relatively large savings cooperative among the approximately 1,400 savings cooperatives, and is ranked the top 50 of all savings cooperatives.

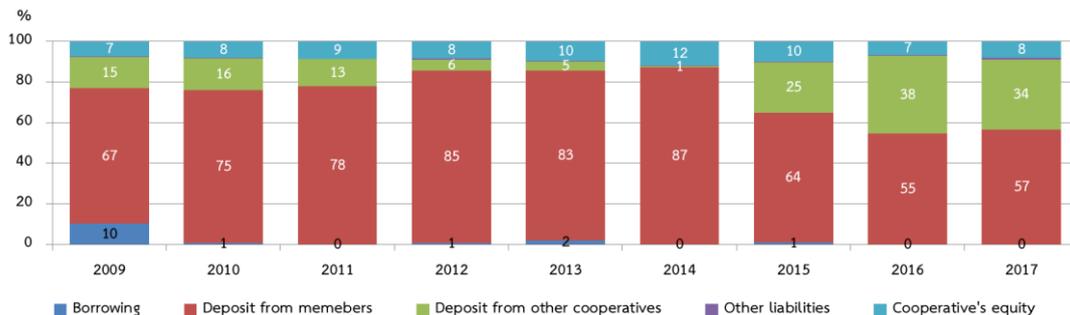
KEY OPERATING PERFORMANCE

Chart 1: PHSC’s Asset Structure



Source: PHSC

Chart 2: PHSC’s Funding Structure



Source: PHSC

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS
Unit: Bt million

	-----Year Ended 30 September-----				
	2017	2016	2015	2014	2013
Total assets	18,840	16,761	9,265	6,126	5,277
Total loans	10,714	8,993	4,903	3,279	2,756
Total investment in securities	4,127	3,194	2,060	1,540	1,389
Allowance for doubtful accounts	0	0	0	0	0
Deposits	17,713	15,555	8,222	5,381	4,647
Borrowings	0	0	100	0	114
Cooperative's equity	1,449	1,111	908	731	508
Net interest and dividend income	155	129	109	108	61
Bad debts and doubtful accounts	0	0	0	0	0
Non-interest income	81	55	28	50	25
Operating expenses	9	10	9	11	13
Net income	227	174	128	148	73

Unit: %

	-----Year Ended 30 September-----				
	2017	2016	2015	2014	2013
Profitability					
Net-interest and dividend income/average assets	0.87	0.99	1.42	1.90	1.22
Non-interest income/average assets	0.45	0.42	0.36	0.88	0.51
Operating expenses/total income	1.25	1.98	2.69	3.55	5.31
Return on average assets	1.28	1.34	1.66	2.59	1.48
Return on average equity	17.74	17.25	15.60	23.82	16.26
Asset Quality					
Non-performing loans/total loans	0.00	0.00	0.00	0.00	0.00
Bad-dents and doubtful accounts/average loans	0.00	0.00	0.00	0.00	0.00
Allowance for doubtful accounts/total loans	0.00	0.00	0.00	0.00	0.00
Allowance for doubtful accounts/non-performing loans	0.00	0.00	0.00	0.00	0.00
Capitalization					
Cooperative's equity/total assets	7.69	6.63	9.80	11.93	9.63
Cooperative's equity/total loans	13.52	12.35	18.52	22.28	18.43
Liquidity					
Total loans/total adjusted deposits	59.57	55.49	55.37	56.39	53.95
Total loans/total assets	44.87	47.68	48.91	48.57	48.88
Liquid assets/total adjusted deposits	56.87	53.66	52.92	53.52	52.22
Liquid assets/total assets	42.83	46.11	46.75	46.11	47.31

Police General Hospital Saving and Credit Cooperative Ltd. (PHSC)

Company Rating:	BBB+
Rating Outlook:	Stable

TRIS Rating Co., Ltd.

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