

SAVING AND CREDIT OF VAJIRA COOPERATIVE LTD.

No. 159/2023
29 August 2023

FINANCIAL INSTITUTIONS

Issuer Rating: BBB+
Outlook: Stable

Last Review Date: 10/08/22

Issuer Rating History:

Date	Rating	Outlook/Alert
25/08/17	BBB+	Stable

RATIONALE

TRIS Rating affirms the issuer rating on Saving and Credit of Vajira Cooperative Ltd. (VJRC) at “BBB+” with a “stable” outlook. The rating reflects VJRC’s satisfactory operating performance, its solid member base, high loan quality, and the competitive edge of savings cooperatives from tax privileges and priority claims against debtors under the savings cooperative law. However, the rating is constrained by VJRC’s asset and liability duration mismatches, its loan concentration, as well as in our view, the inadequate regulatory supervision of savings cooperatives in general.

The rating also factors in VJRC’s readiness to cope and comply with regulatory changes following the enactment of new legislation governing the operations of savings cooperatives.

KEY RATING CONSIDERATIONS

Savings cooperatives enjoy privileges

Under the new law, the privileges granted to savings cooperatives in the forms of tax exemptions and priority claims against debtors remain unchanged. Savings cooperatives and their respective members are exempt from interest savings tax, value added tax, and tax on investment returns. The law also stipulates that a primary savings cooperative has priority claim over any other creditors to receive interest and repayments from its debtors. The priority claim privilege is an important competitive advantage over other lending institutions in lending to cooperative members. Most of the loans extended to ordinary members of primary savings cooperatives are under an arrangement whereby the borrower’s employer deducts the interest and principal installments from the borrower’s monthly salary. This explains the high loan quality and low credit costs of most primary savings cooperatives.

Maintains robust equity, member bases

In our view, VJRC has an adequate capital position as supported by the ratio of equity to total assets standing at 26.6% at the end of fiscal year (FY) 2022 (year-ended 30 September 2022). The majority of VJRC’s ordinary members are employees of government entities with good credit profiles. The high job security and steady monthly income of its members explain the stability of VJRC’s base of ordinary members and their debt repayment ability. The stability of its member base has led to steady increases in VJRC’s capital base as ordinary members are obliged to purchase VJRC’s shares every month. Consequently, VJRC has recorded steady rises in its deposit base, loan portfolio, and paid-up share capital. VJRC’s paid-up share capital rose continuously to THB4.1 billion at the end of FY2022, from THB3.2 billion at the end of FY2017, a compound annual growth rate (CAGR) of 6%.

However, the total equity to assets ratio stood at 27% at the end of fiscal year 2022 (ended September 30, 2022), down from 29% at the end of fiscal year 2021 (ended September 30, 2021). This was due to the unrealized losses from fixed-income debentures investment affected by increases in interest rates. In this regard, TRIS Rating expects VJRC will adopt prudent investment policies going forward as significant unrealized investment losses may weaken the capital base of VJRC.

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Liquidity remains adequate despite duration mismatches

In our view, VJRC has significant mismatches in the maturities of its assets and liabilities, stemming from its short-term borrowings secured by the pledging of its investment securities to keep its funding costs low. As of March 2023, its short-term borrowings accounted for approximately 12% of the sum of total liabilities and equity. In contrast, only 1% of VJRC's total assets were short-term assets.

We view these mismatches as a significant risk in VJRC's asset and liability management, due to the refinancing risk of short-term borrowings. In addition, we also view wholesale funding from financial institutions to be a less stable source of VJRC's funding than funds from members' deposits and members' equity. However, VJRC does have an investment portfolio large enough to cover all its external short-term borrowings, which helps mitigate liquidity risk. We expect VJRC to maintain its conservative investment policy, with no material concentration risk to a specific group of securities or significant investment in riskier classes of assets. VJRC ended March 2023 with a liquidity ratio of around 14.0%, higher than the current liquidity reserve requirement of 1%.

Concentration in loans to other savings cooperatives

In our view, VJRC is exposed to significant loan concentration risk. This is due to its high exposure of lending to other savings cooperatives. Loans to other cooperatives accounted for 78% of total loans at the end of September 2022. Of the total loans to other cooperatives, around 50% were extended to the 10 largest cooperative borrowers. The large credit exposure to other cooperatives stems from VJRC's net-lender position as the amount of deposits it receives from members well exceeds the amount of loans extended to its members. VJRC primarily lends the excess funds to other savings cooperatives. VJRC expects loan extensions to other cooperatives to yield higher returns than from the investment portfolio. However, the concentration risk is mitigated by VJRC's stringent and conservative lending criteria.

We expect VJRC's asset quality to remain high. We believe VJRC has a prudent lending policy, as evidenced by its low ratio of non-performing loans (NPL, or loans more than 90 days overdue). VJRC reported an NPL ratio of 0.5% of its total loans at the end of FY2022, similar to the same period last year and still considered a relatively low ratio. We expect that VJRC will continue to maintain its prudent credit risk policies.

Coping, complying effectively with new regulations

VJRC has coped and complied effectively with the new regulations. The law is basically designed to ensure tighter controls over the deposit taking, lending, and investment activities of savings cooperatives. We view the new law as an important step in alleviating concerns over the long-term stability of savings cooperatives that form an important part of Thailand's financial system.

Nevertheless, we expect the new law will constrain opportunities for growth and weaken VJRC's financial performance in the short term. For instance, more stringent lending, reserve requirements for liquidity and loan losses under the law as well as investment restrictions will mean less flexibility in VJRC's investment activities and lower returns on assets. However, we do not expect the potential impact on profitability to materially affect VJRC's financial strength. On the other hand, the new requirements will likely strengthen VJRC's risk management, and thus enhance its long-term stability.

Inadequate regulatory supervision

Savings cooperatives are not subject to the same degree of close supervision and rigorous examination as banking institutions. In our view, this is the major weakness constraining the credit standings of savings cooperatives in Thailand. Although the new law lays out the framework for tighter controls on savings cooperatives' activities, effective enforcement based on periodic rigorous examinations seems unlikely to happen anytime soon.

BASE-CASE ASSUMPTIONS

TRIS Rating's base-case assumptions for VJRC's performance during FY2023-FY2025 are as follows:

- Loans to decline by 7% in FY2023 and to grow by 3% per annum on average in FY2024-FY2025.
- Equity to grow by 5%-6% per annum on average.
- Spread of around 1%-1.3% per annum.

RATING OUTLOOK

The "stable" outlook reflects our expectation that VJRC will maintain its solid member base and continue delivering satisfactory operating performance to generate acceptable returns for its members. We also expect VJRC to cope well and remain in compliance with the new regulations.

RATING SENSITIVITIES

The prospect of a credit upgrade is constrained by the lack of close supervision and rigorous examination of savings cooperatives in general.

In contrast, a downgrade scenario could arise should there be indications of more aggressive operating and financial policies leading to a deterioration of the financial profile, asset quality or a material loss on investments. In addition, aggressive duration management of assets and liabilities may negatively impact the rating. Any regulatory changes that erode the tax and priority claim privileges currently enjoyed by savings cooperatives could also negatively affect the rating.

ORGANIZATION OVERVIEW

VJRC was established in 1975 as a savings cooperative for the Bangkok Metropolitan Administration’s (BMA) Medical College and Vajira Hospital, currently known as the Faculty of Medicine Vajira Hospital. VJRC also accepts personnel employed at the Kuakarun Faculty of Nursing, the Medical Service Department (MSD) of the BMA, and nine other government hospitals under the supervision of the MSD as ordinary members.

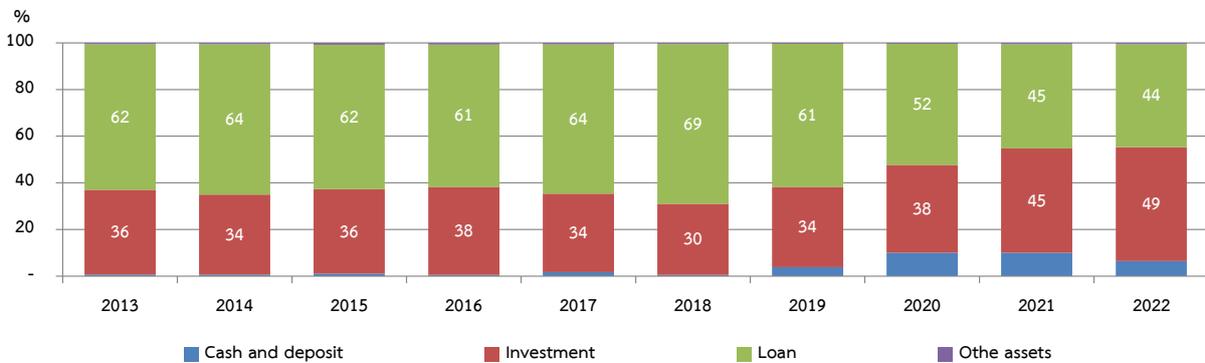
VJRC has strong business and organizational foundations, with a sizable base of assets, stable deposit base, and satisfactory financial performance. VJRC is a large savings cooperative. As of December 2022, in terms of total assets, VJRC was ranked among the top 50 of around 1,400 savings cooperatives in Thailand. VJRC’s total assets were THB20.9 billion as of March 2023.

As is the nature of a savings cooperative, VJRC provides a limited range of financial services for its members, such as taking deposits and extending loans. VJRC also provides basic welfare benefits, like other large and long-established savings cooperatives, to encourage its members to maintain membership.

VJRC has affiliate members as well as ordinary members. Qualified affiliate members are people who have a relationship with an ordinary member or those previously employed at the Faculty of Medicine Vajira Hospital or its affiliates. Deposits and outstanding loans from affiliate members remain relatively small.

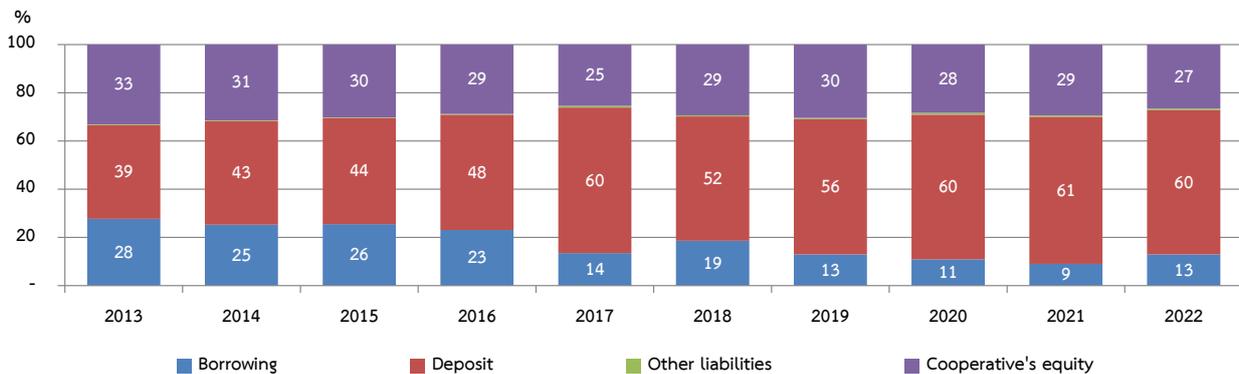
KEY OPERATING PERFORMANCE

Chart 1: VJRC’s Asset Structure



Source: VJRC

Chart 2: VJRC’s Funding Structure



Source: VJRC

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS

Unit: Mil. THB

	----- Year Ended 30 September -----				
	2022	2021	2020	2019	2018
Total assets	21,219	20,063	19,620	17,850	16,855
Total loans	9,416	9,016	10,213	10,986	11,597
Total investment in securities	10,347	8,967	7,388	6,141	5,128
Allowance for doubtful accounts	47	48	48	48	46
Deposits	12,705	12,236	11,763	10,023	8,699
Borrowings	2,747	1,815	2,153	2,313	3,141
Equity	5,638	5,898	5,555	5,437	4,937
Net interest and dividend income	383	358	359	362	341
Bad debts and doubtful accounts	(1)	(0)	0	16	20
Non-interest income	7	2	1	50	39
Operating expenses	26	40 *	41	39	42
Net income	355	320	319	373	338

* Operating expenses excluding THB0.5 million in provision to cover losses from investing in the senior unsecured debentures of Thai Airways International PLC (THAI)

Unit: %

	----- Year Ended 30 September -----				
	2022	2021	2020	2019	2018
Profitability					
Net-interest and dividend income/average assets	1.85	1.81	1.92	2.09	1.94
Non-interest income/average assets	0.03	0.01	0.01	0.29	0.22
Operating expenses/total income	4.76	5.86 *	5.39	5.12	5.57
Return on average assets	1.72	1.61	1.70	2.15	1.92
Return on average equity	6.16	5.58	5.81	7.19	7.04
Asset Quality					
Non-performing loans/total loans	0.50	0.53	0.47	0.44	0.43
Bad-debts and doubtful accounts/average loans	(0.01)	(0.00)	0.00	0.15	0.17
Allowance for doubtful accounts/total loans	0.50	0.53	0.47	0.44	0.40
Allowance for doubtful accounts/non-performing loans	100.00	100.00	100.00	100.00	92.66
Capitalization					
Equity/total assets	26.57	29.40	28.32	30.46	29.29
Equity/total loans	60.17	65.76	54.65	49.70	42.74
Funding and Liquidity					
Member deposit/total funding	73.77	75.57	81.85	73.81	69.27
Liquid assets/(deposits+borrowings+paid-up stocks)	60.04	61.28	53.24	43.20	34.54

* Operating expenses excluding THB0.5 million in provision to cover losses from investing in the senior unsecured debentures of Thai Airways International PLC (THAI)

RELATED CRITERIA

- Savings Cooperative Rating Methodology, 28 August 2023

Saving and Credit of Vajira Cooperative Ltd. (VJRC)

Issuer Rating:	BBB+
Rating Outlook:	Stable

TRIS Rating Co., Ltd.

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