

LAND AND HOUSES SECURITIES PLC

No. 21/2021
9 March 2021

FINANCIAL INSTITUTIONS

Company Rating: BBB
Outlook: Stable

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RATIONALE

TRIS Rating assigns the company rating to Land and Houses Securities PLC (LHS) at “BBB” with a “stable” outlook. The rating reflects the company’s status as a strategically important subsidiary of LH Financial Group PLC (LHFG). The company’s standalone credit profile also takes into consideration the company’s modest market position in the securities business, reliance on investment income, moderate capitalization and earnings, adequate risk profile, and sufficient funding and liquidity.

KEY RATING CONSIDERATIONS

A strategically important subsidiary of LHFG

We view LHS as a strategically important subsidiary of LHFG. The company is wholly owned and closely monitored by LHFG. LHS is also part of the group strategy, performing a role as a securities arm and collaborating with the group’s core subsidiaries, Land and Houses Bank PLC (LHBANK) and LH Fund (LHFUND), to cross sell products and services to their clients.

Although this is only the early stage of collaborations, there have been some signs of progress following product launches in recent years. Last year, Lombard loans (dubbed as “Wealth Lending”) were offered to LHBANK’s clients in addition to private funds and wealth advisory services. Apart from its role as a securities company, LHS also fulfills its strategic role as an investment arm, helping to generate sizable dividend income from investment activities.

The Group has a long-term commitment to support LHS as demonstrated through financial support, including capital injections and long-term credit lines from LHBANK. LHS’s reputation is also closely linked with the Group’s reputation given the shared brand name.

We view the additional rating uplift from group support to be limited over the medium term. For LHS’s group status to be further enhanced requires significant improvements in group collaborations and meaningful revenue contributions to the Group.

Modest market presence in securities business

The company’s business position remains constrained by its limited market presence across business lines in the securities business. For example, its securities brokerage revenue share remained small at 0.7% for the first six months of 2020, ranked 30th among 38 brokerage firms in the industry. The company’s derivatives brokerage revenue share was also modest at 0.4% for the first six months of 2020, ranked 30th among peers. Its less-comprehensive product mix and services remain a constraint to its competitive position and ability to attract new clients onto its platform.

Nevertheless, we expect the company’s market position in the securities business to gradually improve over the next few years. This is based on the condition that group collaborations continue to progress. The company’s planned expansion into products aligned with the demands of the Group’s client base should help enhance its business volumes and market presence in the securities business over the medium term.

Reliance on investment income

We expect the company's revenue diversification to gradually improve in the longer term as revenue contributions from its core business are expected to increase as a result of its business expansion plan. In 2020, interest and dividend income contributed 60% of the company's total revenue, which was a decrease from 63% in 2019 thanks to the revenue growth of its securities business. The revenue contribution from brokerage fees increased to 33% in 2020 from 26% in 2019.

In the medium term, the company still relies on dividend income from investment portfolios as a major revenue source. This continues to weigh on its standalone rating. Although the dividend income was relatively less volatile than revenues from the securities business, we view the current revenue structure as not representing its business strength as a securities brokerage company but rather as an investment arm of LHFG. Also, the revenue concentration exposes the company's earnings to market risk particularly during extreme market volatility.

Moderate capital, leverage, and earnings

The company's capital and leverage improved due to LHFG's capital injection of THB955 million in 2020 and the scaling back of investment activities. As a result, its risk-adjusted capital (RAC) ratio increased to 5.8% in 2020 from 3.4% in 2019. We expect the company's capital and leverage to gradually strengthen and hover around 6% over the next few years as we expect the company to limit its investment portfolio while gradually expanding its equity base with incremental retained earnings.

LHS's earnings capacity remains moderate with a ratio of earnings before taxes to risk-weighted assets (EBT/RWAs) of 60-70 basis points (bps). This has been supported by its well-controlled operating costs. For the first six months of 2020, the company's ratio of operating expenses to net revenue at 39.1% remained significantly lower than the industry average of 63.7%. We believe further cost reduction is difficult, any earning improvement would need to stem from ongoing business expansion and group collaborations.

Adequate risk profile

We consider the company to have an acceptable risk profile as it complies with the risk control policies of LHFG, a financial group regulated by the Bank of Thailand (BOT). We also expect the company to maintain its prudent credit underwriting standards and strict margin call enforcement that should help preserve its asset quality over the next few years.

We view the company as having low risk appetite in general given its cautious business expansion strategy. However, the company's exposure to market risk due to its sizable investment portfolio remains a rating constraint. Most investments were in unit trusts that typically yield stable dividend income. However, these unit trusts when marked to market during extreme stock market volatility has proven to have adverse impact on capital position rising from the company's Fair Value through Other Comprehensive Income (FVOCI) accounting.

Over the next few years, we expect the company's exposure to market risk to remain under control as the company aims to scale down the investment portfolio, following its parent company guidelines. At the end of December 2020, the company's total investments were THB4 billion, compared with its equity of THB1.5 billion.

Sufficient funding and liquidity underpinned by parent support

We assess the company's funding and liquidity profile as adequate as we believe the company is likely to receive ongoing financial supports from LHFG, its parent company. This should help enhance its financial flexibilities. In addition to the capital injection during 2020, ongoing group supports took the form of credit facilities provided by LHBANK, a core subsidiary of LHFG. At the end of December 2020, the company had credit facilities totaling THB6.7 billion, 97% of which were provided by LHBANK.

Stronger trading volume supported securities brokerage firms' performance in 2020

Thailand's stock market rapidly recovered during the second half of 2020, resulting in a sharp increase in average daily trading value in 2020. As a result, securities brokerage firms in our database reported in aggregate a 12% revenue growth in 2020, compared with revenue contraction by 7% in 2019. The impact from the second wave of the Coronavirus Disease 2019 (COVID-19) outbreak on market sentiment and trading volume thus far has been limited, with daily average trading value remaining strong at THB96.8 billion as of February 2021 compared with THB68.6 billion in 2020. The SET Index also continued to rise, close to the pre-COVID level, buoyed by the improving earnings prospects of the banking sector and the market's anticipation of economic recovery following the recent vaccination rollout in Thailand.

BASE-CASE ASSUMPTIONS

TRIS Rating’s base-case assumptions for LHS’s operations in 2020-2023 are as follows:

- Market share in securities trading value to be around 0.6%.
- Average commission rate to be maintained at approximately 10 bps.
- Ratio of operating expenses to net revenue to hover around 42%.

RATING OUTLOOK

The “stable” outlook reflects our expectation that LHS will remain a strategically important subsidiary of LHFG and will continue to receive financial and/or business support from LHFG. The outlook is also based on our expectation that LHS will gradually improve its revenue contribution from the securities business while maintaining sound financial performance and current level of capitalization.

RATING SENSITIVITIES

An upside on LHS’s standalone credit profile could materialize if there were a material improvement in recurring revenue from its core securities business, and its RAC ratio rises above 6% for a sustained period. Conversely, the rating and/or outlook could be revised downward if the company’s financial performance deteriorates significantly, and its RAC falls below 3% for two consecutive years. The rating and/or outlook may also be revised should there be any changes in TRIS Rating’s view of the group status of LHS to LHFG.

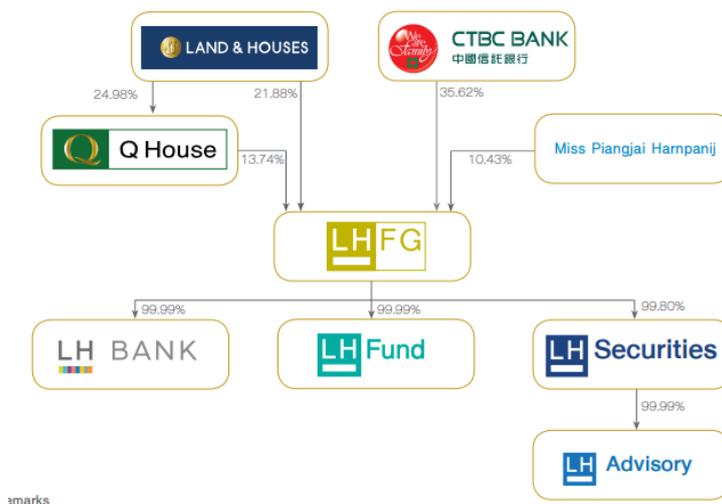
COMPANY OVERVIEW

LHS was formerly CIMB Securities International Ptd., Ltd. (CSI). After acquiring SICCO Securities PLC, which was established on 28 October 1998, CSI changed its name to CIMB Securities International (Thailand) PLC (CIMBI) in September 2011. All CIMBI’s businesses were then transferred to CIMB Securities (Thailand) Co., Ltd. (CIMBS) to integrate all resources, including brokerage accounts, and expand its business.

LHFG then purchased 99.8% paid-up capital of CIMBI and 99.9% paid-up capital of CIMB Advisory (Thailand) Co., Ltd. via CIMBI on 22 January 2014. On 17 April 2014, the company’s name was changed to Land and Houses Securities PLC (LHS), and the BOT allowed the company to be included in the financial business group on 15 January 2014. LHS started operating under the new name on 29 September 2014.

In March 2020, LHS increased its registered shares by 637,215,030 shares, increasing its total registered shares to 1,274,430,030 shares at par value of THB1 per share. The company then sold additional shares to its existing shareholders at THB1.5 per share, raising its registered capital to THB1,274,430,030.

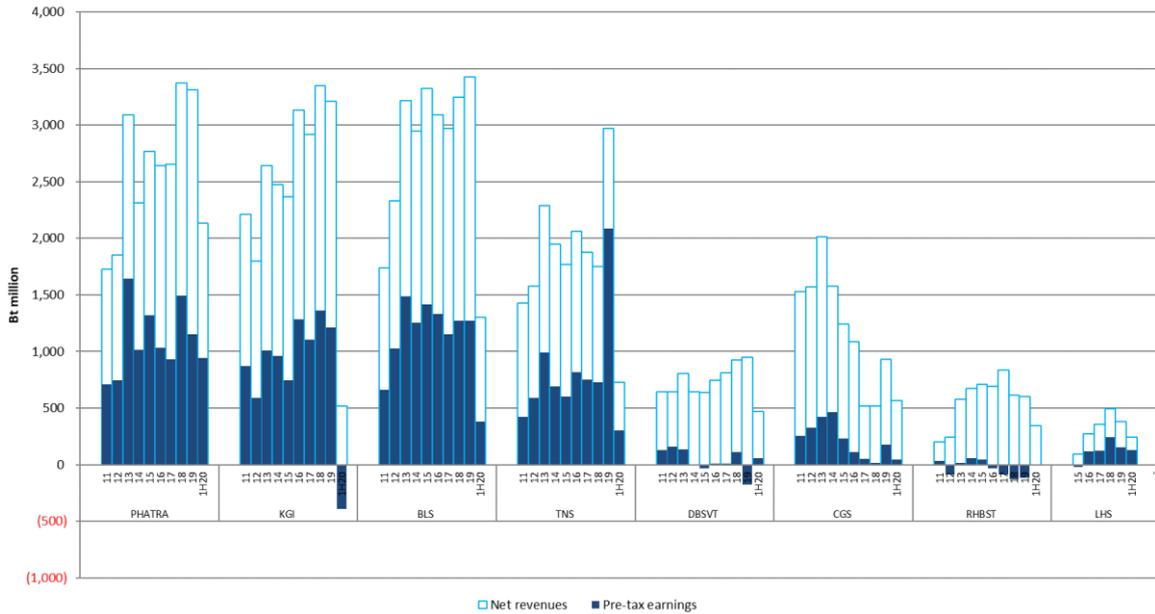
Chart 1: LHFG Group Structure as of Dec 2020



Source: LHS

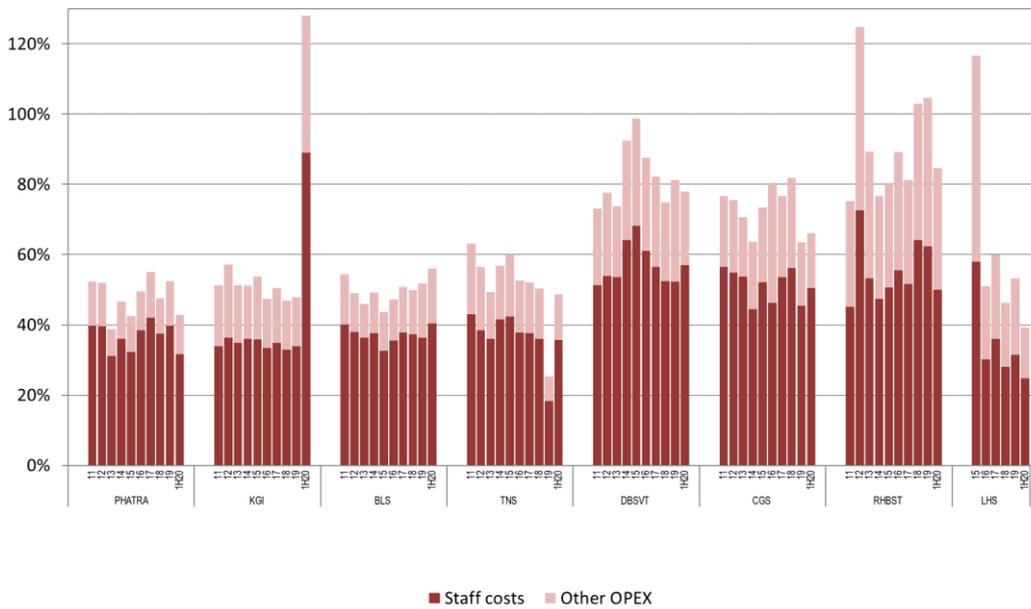
KEY OPERATING PERFORMANCE

Chart 2: Net Revenues and Pre-tax Earnings of Selected Brokers in 2011-1H2020



Sources: Financial statements of each company

Chart 3: 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

	-----Year Ended 31 December -----				
	2020	2019	2018	2017	2016
Total assets	5,680	6,735	4,103	3,588	2,089
Net Investment in securities	4,053	5,769	2,883	2,031	1,438
Total securities business receivables and accrued interest receivables	1,291	735	1,040	1,347	444
Allowance for doubtful accounts*	8	3	-	-	-
Total debts	3,840	5,412	2,600	1,900	765
Shareholders' equity	1,511	1,220	1,264	1,240	1,118
Net securities business income	451	359	470	332	256
Total income	570	505	565	384	297
Operating expenses	188	202	228	212	140
Interest expenses	90	125	73	31	23
Net income	220	142	209	105	106

Unit: %

	-----Year Ended 31 December -----				
	2020	2019	2018	2017	2016
Profitability					
Brokerage fees/total revenues	32.8	26.3	29.2	37.3	30.5
Fees and services income/total revenues	0.3	0.5	0.2	0.4	0.9
Gain (loss) from trading/total revenues	0.0	1.8	27.4	28.1	23.9
Operating expenses/net revenues	39.1	53.3	46.3	59.9	51.0
Pre-tax margin	54.1	40.9	49.4	34.4	43.7
Return on average assets	3.6	2.6	5.4	3.7	6.7
Earning before taxes/risk-weighted assets	0.7	0.5	1.4	1.1	1.9
Asset Quality					
Classified receivables/gross securities business receivables	1.8	3.5	0.0	0.0	0.0
Allowance for doubtful accounts*/gross securities business receivables	0.6	0.4	0.0	0.0	0.0
Credit costs (reversal)	0.5	0.3	0.0	0.0	0.0
Capitalization					
Leverage ratio	38.2	21.6	32.8	31.6	49.4
Risk-adjusted capital	5.8	3.4	6.2	8.1	12.2
Funding and Liquidity					
Gross stable funding ratio	55.3	35.7	63.4	73.1	110.2
Liquidity coverage metric (times)	0.5	0.6	0.6	0.6	1.0

** Allowance for impairment losses under TFRS 9*
RELATED CRITERIA

- Group Rating Methodology, 13 January 2021
- Securities Company Rating Methodology, 9 April 2020

Land and Houses Securities PLC (LHS)

Company Rating:	BBB
Rating Outlook:	Stable

TRIS Rating Co., Ltd.

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