

# LH FINANCIAL GROUP PLC

No. 30/2024  
21 March 2024

## FINANCIAL INSTITUTIONS

**Company Rating:** AA+  
**Outlook:** Stable

**Last Review Date:** 21/03/23

### Company Rating History:

Date	Rating	Outlook/Alert
21/03/23	A-	Stable
15/03/22	BBB+	Negative
26/04/19	BBB+	Stable
09/05/18	BBB+	Positive

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## RATIONALE

TRIS Rating upgrades the company rating on LH Financial Group PLC (LHFG) to “AA+/Stable” from “A-/Stable”. The upgrade reflects our upward revision of LHFG Group’s status from ‘strategically important’ to ‘highly strategic’ entity of the controlling parent, CTBC Bank Co., Ltd. (rated “A/Stable” by S&P Global Ratings).

As a non-operating holding company of the group, the rating on LHFG is one notch below the group credit profile (GCP), assessed at ‘aaa’, due to structural subordination.

The revision of LHFG Group’ status is based on our view of increased strategic and operational integration compared to that observed in 2023. It also incorporates our expectation that the group is likely to receive business and financial support along with extraordinary support in times of need from the CTBC Bank.

We maintain our assessment of the stand-alone credit profile (SACP) of LHFG Group at “bbb”, which reflects the consolidated credit profile of the core operating bank, Land and Houses Bank PLC (LHBANK) as well as other entities including Land and Houses Fund Management Co., LTD (LH Fund). and Land and Houses Securities (LHS).

## KEY RATING CONSIDERATIONS

### Highly strategic subsidiary of CTBC Bank

LHFG’s “highly strategic” group status reflects our view that CTBC Bank will continue in its strong long-term commitment to provide business and financial support to LHFG Group. We also expect CTBC Bank to provide extraordinary support in times of financial distress.

CTBC Bank remains the largest controlling shareholder of LHFG, with a 46.6% equity holding. LHFG currently stands as the largest overseas investment by the CTBC Group. The company plays an important role in fulfilling the CTBC Group’s strategy to expand its global footprint, especially in Southeast Asia. The investment in LHFG is part of the group’s ambition to establish itself as a top-tier regional bank in Asia. This aligns with the objectives of the Taiwanese government’s New Southbound Policy.

CTBC Bank has control over LHFG through the appointment of six out of 11 LHFG’s board members to oversee the company’s business strategy and operations. The financial statement of CTBC Bank consolidates LHFG’s performance. Also, key senior management positions are appointed by CTBC Bank.

Its core operating bank, LH Bank, also adopts a matrix organizational structure with dotted line reporting system where heads of business units (BU) and functional units (FU) are required to report to the respective global BU and FU heads of CTBC Bank. There has also been increased integration, particularly in risk management policies that are now completely aligned with those of CTBC Bank.

In terms of financial support, CTBC Bank currently provides USD375 million interbank funding facilities to LHBANK to support its funding needs.

### **Structural subordination due to NOHC status**

LHFG operates commercial banking business through its wholly-owned banking subsidiary, LHBANK, whose consolidated assets represents around 95% of the group's consolidated assets. Other operating entities within the group comprise LH Fund and LHS. The rating assigned to LHFG is one notch below the GCP of LHFG Group. This reflects the structural subordination of LHFG's obligations with respect to claims against the operating assets at subsidiary level. As a non-operating financial holding company (NOHC), LHFG mainly relies on dividends from LHBANK to service its obligations. There is also the risk of regulatory intervention surrounding payments of dividends from LHBANK to LHFG in a stress scenario.

### **LHBANK's banking franchise is modest**

LHBANK's credit profile represents the SACP of LHFG Group. LHBANK has a relatively modest scale of operations in the Thai banking industry. As of end-2023, LHBANK held the eighth position among Thai commercial banks in terms of asset size, with market shares of 1.4% in terms of both loans and deposits. With business support from CTBC Bank, LHBANK is leveraging the extensive network and expertise of CTBC Bank in serving Taiwanese customers. Although the proportion of loans to Taiwanese corporate customers remains moderate, we expect it to gradually increase over the next five years. This is based on our assumption of an expanding customer base, increasing utilization of working capital loan facilities, and a gradual rise in foreign direct investment from Taiwan. As of February 2024, loans to Taiwanese customers accounted for 5% of total loans.

### **Strong loan growth, investment revaluation erodes capital base**

We maintain our assessment of LHFG's capital position as 'adequate' despite its weakening capital position, as measured by the consolidated core equity Tier 1 (CET-1) ratio. The ratio declined to 12.4% at end-2023, down from 13.4% at end-2022. This was due to its robust credit expansion of 8% in 2023, compared with the commercial banks' average of -0.3%. The CET-1 was also pressured by the revaluation of its investment in property funds and real estate investment trusts, which have been marked to market through other comprehensive income (OCI). Based on our base-case assumptions, we expect its CET-1 ratio to stay at around 12% over the next three years, taking into account our 8%-10% loan growth assumption and dividend payout ratio of 15%.

### **Slow recovery in profitability to continue**

In our view, LHFG has encountered challenges of slow profit recovery over the past three years. This is likely to continue. LHFG's consolidated return on average assets (ROAA) was 0.7% in 2023, lagging the industry average of 1.3%. The company's profitability has been pressured by higher credit costs and investments in the retail operating platform at LHBANK and moderate profitability at LH Fund and LHS. We project LHFG's consolidated ROAA to stay within the 0.7%-0.8% range in 2024-2026.

### **Manageable asset quality, strong reserves**

LHFG's asset quality reflects that of LHBANK. The bank's asset quality improved in 2023. Despite a slight uptick in the non-performing loan (NPL) ratio (excluding interbank assets) to 2.7% at end-2023 from 2.4% at end-2022, the stage-2 loan ratio decreased substantially. The ratio dropped to 3% from 5% at end-2022, driven by improvement in the corporate and SME segments. Loans under relief programs also fell significantly to 9.9% of total loans from 18.8% at end-2022. Although we expect LHBANK's NPL ratio to hover above 3% over the next three years due to slippages of stage-2 corporate loans, credit cost is unlikely to increase significantly as we view LHBANK already having sufficient reserves. Its NPL coverage was at a robust level of 219% as of the end of 2023, surpassing the industry average of 179%.

### **Reliance on high-cost retail deposits**

LHFG's funding profile mirrors that of LHBANK's deposit franchise, which continues to constrain its credit profile. We expect its funding profile will remain below the average of Thai commercial banks. Current and savings accounts (CASA) to total deposits dropped significantly to 24% at end-2023 from 37% at end-2022. Similar to other smaller banks, LHBANK relies heavily on fixed deposits from wealthy individuals, which raises deposit costs to higher than industry average. On a positive note, there is slightly less reliance on wholesale funding. As of end-2023, deposits represented 89% of total funding, up from 86% at end-2021.

### **Sufficient liquidity position**

We expect LHFG's liquidity profile to remain sufficient over the next 12 months, mirroring that of LHBANK. The bank's liquidity coverage ratio (LCR) stood at an average of 142% in the second quarter of 2023. This was above the regulatory requirement of 100% albeit weaker than the average for Thai banks of 204% reported by the Bank of Thailand (BOT).

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## BASE-CASE ASSUMPTIONS

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Our base-case assumptions for LHFG’s operation during 2024-2026 are as follows:

- Loan growth: 8%-10% per annum
- Net interest margin: 2.3%-2.4%
- Cost-to-income: 46.5%
- Credit cost: 0.7%-0.9%
- NPL ratio (excluding interbank assets): 3.0%-3.6%

## RATING OUTLOOK

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The “stable” outlook reflects our expectation that LHFG will maintain its group status as a highly strategic subsidiary of CTBC Bank and continue to receive strong support from its parent bank. We also expect LHFG to continuously expand its banking franchise while maintaining capital and asset quality. At the same time, we expect LHFG to maintain its consolidated CET-1 ratio above 12%.

## RATING SENSITIVITIES

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The credit rating and/or outlook of LHFG could change if the credit profile of the CTBC Bank Group changes or our view of LHFG’s group status changes. LHFG’s credit upside is limited in the near term. Conversely, a rating downgrade could occur if there were any reduction in CTBC Bank’s stake in LHFG and/or financial performance or operational integration weakens materially for a prolonged period that leads us to conclude that LHFG’s status to CTBC Bank is lower than ‘highly strategic’.

## COMPANY OVERVIEW

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LHFG was established on 22 April 2009 as an NOHC under the BOT’s consolidated supervision principle. LHBANK was set up as a subsidiary under the solo consolidation group, while LH Fund was a subsidiary outside the solo consolidation group. After restructuring, the shareholders of LHBANK became the shareholders of LHFG, which holds 99.99% of the paid-up shares of LHBANK. LHFG acquired a 99.80% stake in CIMB International (Thailand) PLC and a 99.99% stake in CIMB Advisory (Thailand) Co., Ltd. from CIMB International (Thailand). The two companies were renamed Land and Houses Securities PLC (LHS) and Land and Houses Advisory Co., Ltd. (LH Advisory). On 1 March 2016, LHFG also acquired a 99.99% stake in LH Fund from LHBANK as part of a group restructuring.

On 27 July 2017, CTBC Bank, a banking subsidiary of CTBC Financial Holding Co., Ltd. (CTBC FHC) in Taiwan, acquired 35.6% of LHFG. The combined shareholding of Land and Houses PLC (LH) and Quality Houses PLC (QH) in LHFG, therefore, was reduced to 35.6%. Other key subsidiaries under CTBC FHC include life insurance, securities, venture capital, and asset management. CTBC Bank is well-positioned in wealth management and credit card services, and is well-established in corporate banking, offering products like trade finance, treasury services, transaction banking, and offshore finances. CTBC Bank is rated “A/Stable” by S&P Global Ratings and “A2/Stable” by Moody’s Investors Service (Moody’s).

On 8 September 2021, CTBC Bank acquired additional shares in LHFG, in aggregate of 10.99% of the total issued and voting shares. Consequently, CTBC Bank holds LHFG’s shares in aggregate of 46.61% of the total issued and voting shares. LHFG also became a subsidiary of CTBC Bank after gaining the majority seats of LHFG’s board of directors.

**FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS<sup>1</sup>**
*Unit: Mil. THB*

	-----Year Ended 31 December -----				
	2023	2022	2021	2020	2019
Total assets	323,323	301,556	264,688	249,312	240,731
Average assets	312,440	283,096	257,000	245,021	243,332
Interbank and money market items	30,724	33,051	34,056	32,367	18,569
Investments	49,557	54,423	53,655	55,683	66,289
Loans and receivables	228,698	207,527	171,817	156,217	152,041
Loan loss reserves	13,782	11,598	9,151	6,014	4,017
Deposits	251,437	231,408	192,499	182,720	164,985
Borrowings <sup>2</sup>	30,734	29,314	31,049	23,731	32,273
Shareholders' equities	35,961	36,871	38,199	38,631	41,163
Average equities	36,416	37,535	38,415	39,897	40,436
Net interest income	6,943	6,195	5,439	4,726	4,486
Net fees and service income	691	753	855	728	729
Non-interest income <sup>3</sup>	1,787	1,929	2,636	3,022	3,418
Total revenue	8,730	8,123	8,075	7,747	7,904
Operating expenses <sup>4</sup>	4,047	3,590	3,223	2,997	3,005
Pre-provision operating profit (PPOP)	4,683	4,534	4,852	4,750	4,899
Expected credit loss	2,163	2,704	3,275	2,304	1,093
Net income	2,096	1,579	1,384	2,057	3,215

- 1 Consolidated financial statements
- 2 Including interbank and money market
- 3 Net of fee and service expenses
- 4 Excluding fee and service expenses

Unit: %

	-----Year Ended 31 December -----				
	2023	2022	2021	2020	2019
<b>Earnings</b>					
Return on average assets	0.67	0.56	0.54	0.84	1.32
Net interest margins	2.23	2.17	2.11	1.93	1.84
Risk-adjusted net interest margins	1.54	1.23	0.84	0.99	1.40
Net interest income/average assets	2.22	2.19	2.12	1.93	1.84
Non-interest income <sup>5</sup> /average assets	0.57	0.68	1.03	1.23	1.40
Net fees and service income/total revenue	7.91	9.27	10.59	9.39	9.23
Cost-to-income	46.36	44.19	39.91	38.69	38.02
<b>Capitalization</b>					
CET-1 ratio <sup>6</sup>	12.36	13.44	15.91	16.66	15.08
Total capital ratio <sup>6</sup>	14.42	15.36	17.95	19.18	17.36
CET-1/Total capital <sup>6</sup>	85.74	87.52	88.64	86.87	86.87
<b>Asset Quality</b>					
Credit costs	95	137	193	145	69
Non-performing loans/total loans <sup>7</sup>	2.64	2.43	2.86	3.33	1.78
Loan loss reserves/non-performing loans <sup>7</sup>	218.81	220.99	179.10	112.04	144.73
<b>Funding &amp; Liquidity</b>					
CASA/total deposit <sup>8</sup>	24.08	37.14	50.68	50.18	40.16
Loan/total deposits <sup>8</sup>	94.87	93.34	92.86	88.31	94.46
Deposits/total funding	89.11	88.76	86.11	88.51	83.64
Liquidity coverage ratio	n.a.	177	131	144	140
Liquid assets/total assets	25.04	29.24	33.42	35.65	35.93
Liquid assets/total deposits <sup>9</sup>	29.63	34.54	41.78	45.55	49.30

5 Net of fee and service expenses

6 Consolidated basis

7 Based on reported NPL, excluding accrued interests and interbank assets

8 Excluding bills of exchange and interbank borrowing

9 Including bills of exchange and interbank borrowing

n.a. Not available

## RELATED CRITERIA

- Financial Institution Rating Methodology, 24 November 2023

- Group Rating Methodology, 7 September 2022

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**LH Financial Group PLC (LHFG)**

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<b>Company Rating:</b>	AA+
<b>Rating Outlook:</b>	Stable

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**TRIS Rating Co., Ltd.**

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