

KIATNAKIN BANK PLC

No. 22/2012

11 April 2012

Company Rating:	A-	
Outlook:	Positive	
New Issue Rating:	A-	
Rating History:		
Date	Company	Issue (Unsecured/ Subordinated)
31/03/11	A-/Pos	A-/-
30/11/04	A-/Sta	A-/-
12/07/04	BBB+/Pos	BBB+/-
21/05/02	BBB+	BBB+/-
21/06/00	BBB	BBB/-
06/03/00	BBB/Alert Neg	-
25/11/99	BBB	-

Rating Rationale

TRIS Rating affirms the company and current senior debenture ratings of Kiatnakin Bank PLC (KK) at "A-". At the same time, TRIS Rating assigns a rating of "A-" to KK's proposed issue of up to Bt2,485 million in senior debentures. The ratings reflect the improvement in the bank's business and financial profiles, experienced management team, acceptable risk management practices, improving asset quality, and strong level of capital funds. However, the ratings are constrained by the bank's moderate franchise value, limited distribution network compared with larger banks, and the uncertain movements in private savings caused by a drop in the amount of insured deposits, in accordance with the Deposits Protection Agency Act (DPA). Furthermore, KK's future business growth and profitability might be affected by the changing economic and political environments, as well as intense competition in both the banking and securities businesses.

KK was ranked 11th among 15 Thai commercial banks in terms of total assets, with 1.6% market share in assets, 1.7% in loans, and 0.9% in deposits as of December 2011. KK's core businesses in auto hire-purchase lending, residential project lending, and distressed asset management are well managed, with high levels of management expertise. Despite heavy floods in Thailand in late 2011, KK's loan portfolio expanded by 26% to Bt135.7 billion at the end of December 2011, supported by rising domestic vehicle sales and economic growth during the first three quarters of 2011. Of the total, 74% was hire-purchase lending, while 26% was residential project loans and others. As of December 2011, auto hire-purchase lending rose by 31% to Bt100.8 billion, compared with Bt77.0 billion in 2010. Loans for real estate and construction increased by 13%, from Bt20.6 billion in 2010 to Bt23.3 billion in 2011.

As a part of its growth strategy, in December 2011, KK signed a Memorandum of Agreement for a merger with Phatra Capital PLC (PHATRA). In 2011, PHATRA was ranked eighth among 33 active brokers in terms of trading volume. The collaboration between KK and PHATRA is aimed at the joint establishment of financial services businesses. KK plans to make a tender offer for PHATRA by issuing new ordinary shares of KK to swap with PHATRA's shareholders. The tender offer will take place in the third quarter of 2012. Once the merger is successful, KK should have a greater competitive edge in security brokerage services. The consolidated operating performance of KK could rise, if KK and its affiliates can generate more fee-based income. However, the immediate benefits after the merger are not expected to be significant enough to change KK's credit profile.

As KK has a strategy to expand its business by focusing on good quality assets, the bank has recently imposed more stringent credit policies and underwriting criteria. KK's non-performing loans (NPLs) have consistently fallen, from Bt5.4 billion in 2009 to Bt5.0 billion in 2010 and to Bt4.7 billion in 2011. The ratio of NPLs to total loans has continually improved, tumbling from 6.2% of total loans in 2009 to 4.6% in 2010 and 3.5% in 2011. At the same time, non-performing assets (NPAs; classified loans more than three months past due, plus restructured loans and foreclosed property) were 6.0% of total assets in 2011, down from 9.9% in 2009 and 9.0% in 2010. KK has made loans to sub-prime residential developers which

Contacts:

Phisut Sakulthong
phisut@trisrating.com

Thiti Karoonyanont, CFA
thiti@trisrating.com

Raithiwa Naruemol
raithiwa@tris.co.th

WWW.TRISRATING.COM

CreditUpdate reviews ratings of companies or debt issues that have already been rated by TRIS Rating. The *CreditUpdate* occurs when new debt instruments are issued or if significant events have taken place that may impact a company's current ratings or when current ratings are cancelled. The *CreditUpdate* announces whether a rating has been "upgraded," "downgraded," "affirmed" or "cancelled." The update includes information to supplement the previously published ratings.

CreditUpdates are part of TRIS Rating's monitoring process. TRIS Rating monitors every rating it assigns until either the debt instrument matures or the rating contract ends. To keep the public informed of changing situations, TRIS Rating periodically issues announcements about the credit ratings it monitors.

were considered as high credit risk loans. The bank's NPL ratio for loans to the real estate and construction sectors remained high at 12.4% in 2011. Nonetheless, KK maintains an adequate cushion of capital and allowances for doubtful accounts to absorb the risks from the NPAs. The ratio of NPAs to capital funds plus the allowance for doubtful accounts improved from 0.61 times in 2009 to 0.41 times in 2011. In the meantime, the bank's ratio of allowance for doubtful accounts to NPLs jumped to 108.0% in 2011, from 69.7% in 2009 and 85.1% in 2010. KK may face a rise in NPLs in the aftermath of the flooding in Thailand. However, any increase in NPLs is expected to be temporary and manageable.

KK has been able to generate more income and sustain the high yield from its core businesses, while successfully controlling its operating costs. However, KK's funding cost was higher in 2011, following the rise in market interest rates. The bank also provided more reserves for possible loan losses which arise because of the floods. KK reported a net profit of Bt2,859 million in 2011, up slightly by 1% from Bt2,840 million in 2010. In 2011, the bank's return on average assets (ROAA) and return on average equity (ROAE) were 1.7% and 12.8%, respectively, down from 2.1% and 14.6% in 2010. KK's future profitability may be affected by new regulations requiring an increase in the regulatory fee charges based on deposits and bills of exchange (B/Es). The cost of funds may rise because of a mandated increase in the fees paid to the Bank of Thailand (BOT), in order for the BOT to repay the debt burden of the Financial Institutions Development Fund (FIDF).

In terms of liquidity and funding, KK is exposed to some level of liquidity risk, as the bank has a maturity mismatch for assets and liabilities with less than 12 months duration. KK also relies on wholesale funding, which tends to be a more volatile funding source. As of December 2011, KK's funding structure comprised B/Es, accounting for 49% of total deposits and B/Es, plus time deposits (42%), and current and savings deposits (CASA, 9%). However, KK has a strategy to increase the number of retail accounts in an effort to diversify and stabilize its sources of funding. The upcoming reduction of the maximum amount of insured deposits, from Bt50 million to Bt1 million in August 2012, may affect KK's financial strength and the stability of its funding sources.

KK has a strong capital base, as illustrated by a capital adequacy ratio of 15.4% in 2011, up from 15.2% in 2010. The bank's equity to asset ratio dropped slightly to 12.5% in 2011 from 14.7% in 2010, as the loan portfolio expanded. As KK engages in high risk and high return lending, especially for residential project loans, it is crucial for the bank to maintain a strong capital base and stringent allowances for doubtful accounts. The capital base and allowances can absorb unexpected losses from future downside risks.

Rating Outlook

The "positive" outlook reflects the expectation that KK will be able to continue growing and sustain its profitability in the medium term. The outlook also reflects the bank's ability to control asset quality and maintain a level of capital funds sufficiently to absorb any downside risks arising from uncertainties in the economic and financial environments. Three major concerns remain: the possible effects from the recent floods in Thailand, the risk of KK's retail deposit base becoming unstable after the full implementation of the DPA in August 2012, and a possible rise in the cost of funds. KK's ability to sustain its strengths and to secure stable sources of funds at reasonable prices has yet to be proved.

Kiatnakin Bank PLC (KK)

Company Rating:	A-
Issue Ratings:	
KK127A: Bt2,493 million senior debentures due 2012	A-
KK120A: Bt2,000 million senior debentures due 2012	A-
KK142A: Bt2,905 million senior debentures due 2014	A-
KK16DA: Bt975 million senior debentures due 2016	A-
KK187A: Bt240 million senior debentures due 2018	A-
KK18DA: Bt625 million senior debentures due 2018	A-
KK18DB: Bt10 million senior debentures due 2018	A-
Up to Bt2,485 million senior debentures due within 2014	A-
Rating Outlook:	Positive

TRIS Rating Co., Ltd.

Office of the President, Tel: 0-2231-3011 ext 500 / Silom Complex Building, 24th Floor, 191 Silom Road, Bangkok 10500, Thailand www.trisrating.com

© Copyright 2012, TRIS Rating Co., Ltd. All rights reserved. Any unauthorized use, disclosure, copying, republication, further transmission, dissemination, redistribution or storing for subsequent use for any purpose, in whole or in part, in any form or manner or by any means whatsoever, by any person, of the credit rating reports or information is prohibited. The credit rating is not a statement of fact or a recommendation to buy, sell or hold any debt instruments. It is an expression of opinion regarding credit risks for that instrument or particular company. The opinion expressed in the credit rating does not represent investment or other advice and should therefore not be construed as such. Any rating and information contained in any report written or published by TRIS Rating has been prepared without taking into account any recipient's particular financial needs, circumstances, knowledge and objectives. Therefore, a recipient should assess the appropriateness of such information before making an investment decision based on this information. Information used for the rating has been obtained by TRIS Rating from the company and other sources believed to be reliable. Therefore, TRIS Rating does not guarantee the accuracy, adequacy, or completeness of any such information and will accept no liability for any loss or damage arising from any inaccuracy, inadequacy or incompleteness. Also, TRIS Rating is not responsible for any errors or omissions, the result obtained from, or any actions taken in reliance upon such information. All methodologies used can be found at http://www.trisrating.com/en/rating_information/rating_criteria.html.