

Yuanta Securities Finance Co. Ltd.

2011/02/16

Primary Credit Analyst:	Eva Chou; (886) 2 8722-5822, eva_chou@taiwanratings.com.tw
Secondary Contact:	Eunice Fan; (886) 2 8722-5818, eunice_fan@taiwanratings.com.tw

Current Ratings (2011/01/19)	Counterparty credit rating:	twAA-/Positive/twA-1+
Credit Rating History	2011/01/19	twAA-/Positive/twA-1+
	2007/06/07	twAA-/Stable/twA-1+
	2006/12/01	twAA-/Stable/twA-1
	2005/09/15	twA-/Positive/twA-2

Major Rating Factors**Strengths:**

- Implicit support from the parent Yuanta FHC group
- Adequate capitalization relative to its risk profile
- Satisfactory position in margin lending business

Weaknesses:

- Limited revenue diversity due to constrained business scope on the industry
- Obstacles to grow new business
- Volatile profitability along with Taiwan stock market conditions

Rationale

The ratings on Yuanta Securities Finance Co. Ltd. (Yuanta SFC) reflect the implicit parental support from the Yuanta Financial Holding Co. Ltd. (Yuanta FHC; twA+/Positive/twA-1) group, as well as Yuanta SFC's adequate capitalization and satisfactory market position in Taiwan's securities finance industry. Counterbalancing factors include the company's limited revenue diversity, obstacles to grow new business, and volatile profitability.

The ratings recognize the strong and frequent resource fungibility between the Yuanta group and Yuanta SFC. The company plays an important role as the group's agent margin lending service provider supporting the group's strategic goal to provide a broad securities related services. Yuanta Securities Co. Ltd. (twAA-/Positive/twA-1+) outsourced its margin finance business to Yuanta SFC in 2007 but transferred this back in 2010 as part of the group's strategic move to enhance capital management. Yuanta SFC conducted a capital upstream of Taiwan dollar 16.5 billion to the group in 2011 in tandem with the aforementioned margin lending business transfer.

Yuanta SFC's capitalization is adequate relative to its risk profile, and we do not expect this to significantly change over the next several quarters. The company's ratio of adjusted total equity to assets (considering Yuanta SFC's capital upstream and business transfer in 2010) was 58% at the end of 2010, based on preliminary financials. This was lower than the 2008 level that peaked at 65% due to low market demand for margin lending.

Yuanta SFC has a satisfactory position in Taiwan's margin lending business through its majority control over business sourced from independent agent securities brokers in Taiwan. Yuanta SFC's market share dropped to 6.8% at the end of October 2010 from 20% a year earlier following the group's transfer of its margin-lending business to Yuanta Securities.

Yuanta SFC's revenue streams are limited to its margin lending business, which exposes the company to performance volatility and growth limitation. The sector is highly regulated in Taiwan. Margin lending business generated about 75% of the company's total revenues in the 30 month period up to September 2010.

Yuanta SFC faces obstacles to grow new business as local securities finance companies are mandated to provide margin-lending business to brokerage customers of independent agent securities brokers. There is no solid base for the company to grow new business as the number of such brokers has declined along with the securities industry's ongoing consolidation, though this has slowed since 2008.

Yuanta SFC's profitability is subject to volatile stock market turnover because of its concentration of revenue streams in margin-lending business. The company's return on average assets was 2.8% for the 18 months ended September 2010, up from 1.5% in 2008, mainly thanks to the domestic stock market's recovery.

Enterprise Risk Management

Yuanta SFC has an adequate enterprise risk management framework with adequate risk governance supported by the Yuanta group's proactive management. The company mainly relies on traditional silo-based risk management approaches that are synchronized with its simple business profile.

Outlook

The positive outlook reflects our expectation on the direction of the Yuanta group's credit profile, given Yuanta SFC's core status. The group's credit profile could improve along with enhancement in its earnings profile over the next one to two years. We also expect the group's adequate risk management and capitalization to serve as a good buffer to cushion against potential capital market volatility for the relatively high market risk exposure it faces. Yuanta FHC is likely to follow prudent business strategies and financial policies in pursuing organic growth as well as through M&A activity. On a stand-alone basis, we expect Yuanta SFC's capitalization to remain adequate relative to its risk profile.

We may raise the ratings on Yuanta SFC if Yuanta Securities' earnings profile strengthens further, supported by its leading market position or improved diversification. We may revise the outlook back to stable if we observe a significant weakening in Yuanta Securities' competitiveness or profitability. We may also lower the ratings if the group's capitalization or profitability weakens due to its aggressive growth strategy organically or via M&A activity without adequate business and financial risk controls, or if Yuanta SFC's strategic importance to the group diminishes.

Related Criteria And Articles

- Outlook On Yuanta Financial Holding Co. Ltd. And Key Subsidiaries Revised To Positive On Resilient Earnings Profiles; Ratings Affirmed, published on www.taiwanratings.com/en on Jan. 19, 2011
- Criteria | Financial Institutions| General: Group Methodology, published on www.globalcreditportal.com on April 22, 2009
- Criteria | Financial Institutions | General: Assessing Enterprise Risk Management Practices Of Financial Institutions, published on www.globalcreditportal.com on Sept. 22, 2006
- Criteria | Financial Institutions | Broker-Dealers: Rating Securities Companies, published on www.globalcreditportal.com on June 9, 2004

Yuanta Securities Finance Co. Ltd.					
	--Year Ended Dec. 31--				
(Mil. NT\$)	2010*	2009	2008	2007	2006
Assets	80,850	69,363	47,237	96,088	49,936
% change	16.56	46.84	(50.84)	92.42	11.10
Loans (net)	73,744	60,799	27,848	81,832	34,040
% change	21.29	118.33	(65.97)	140.40	20.10
Total published equity	32,112	32,207	30,516	18,625	16,137
% change	(0.30)	5.54	63.84	15.42	5.49
Adjusted common equity	32,112	32,207	30,516	18,625	16,137
% change	(0.30)	5.54	63.84	15.42	5.49
Adjusted total equity	32,112	32,207	30,516	18,625	16,137
% change	(0.30)	5.54	63.84	15.42	5.49
Revenues	3,501	4,119	3,559	3,910	2,038
% change	13.06	15.73	(8.98)	91.82	24.23
Non-interest expense	1,868	1,937	2,126	2,329	705
% change	28.23	(8.88)	(8.72)	230.48	96.30
Net operating income before loan loss provision (LLP)	1,633	2,181	1,433	1,581	1,333
% change	(0.41)	52.24	(9.35)	18.53	4.04
Pretax income	1,633	2,181	1,433	1,581	1,333
% change	(0.41)	52.24	(9.35)	18.53	196.72
Net income	1,364	1,814	1,058	1,253	1,028
% change	0.05	71.39	(15.54)	21.88	185.44
Profitability (%)					
Revenues/average assets	6.20	7.06	4.97	5.36	4.30
Net interest income/average assets	4.75	4.21	4.47	4.37	3.42
Noninterest income/average assets	1.45	2.86	0.50	0.98	0.88
Noninterest expense/average assets	3.31	3.32	2.97	3.19	1.49
Net operating income before LLP/average assets	2.89	3.74	2.00	2.16	2.81
Net operating income after LLP/average assets	2.89	3.74	2.00	2.16	2.81
Pre-tax profits/average assets	2.89	3.74	2.00	2.16	2.81
Net income/average assets (ROA)	2.42	3.11	1.48	1.72	2.17
Net interest income/revenues	76.60	59.56	89.93	81.67	79.60
Non-interest income/revenues	23.40	40.44	10.07	18.33	20.40
Non-interest expense/revenues	53.35	47.04	59.74	59.57	34.58
Net operating income before LLP/revenues	46.65	52.96	40.26	40.43	65.42
Net operating income after LLP/revenues	46.65	52.96	40.26	40.43	65.42
LLP/revenues	0.00	0.00	0.00	0.00	0.00
Pre tax profits/revenues	46.65	52.96	40.26	40.43	65.42
Net income/revenues	38.97	44.04	29.73	32.05	50.44
Net interest income/average earning assets	4.90	4.48	4.80	4.60	3.65
Net income/average adjusted common equity (ROE)	5.64	5.78	4.31	7.21	6.54
Liquidity (%)					
Customer deposits/all funding base	0.00	0.00	0.00	0.00	0.00
Loans/customer deposits + long-term funds	213.55	163.85	73.68	313.60	216.13
Loans (net)/assets	91.21	87.65	58.95	85.16	68.17
Capital (%)					
Adjusted common equity/assets	39.72	46.43	64.60	19.38	32.32
Adjusted common equity/loans	43.54	52.97	109.58	22.76	47.41

Adjusted total equity+ loan loss reserve/loans (gross)	43.67	53.10	109.53	22.85	48.67
Adjusted total equity/assets	39.72	46.43	64.60	19.38	32.32
Adjusted total equity/loans(net)	43.54	52.97	109.58	22.76	47.41
Asset quality (%)					
Loan loss reserves/loans (gross)	0.23	0.27	0.59	0.12	2.40
Nonperforming assets (gross)/loans (gross) + other real estate	0.02	0.03	0.11	0.02	2.22
Net nonperforming assets/loans + other real estate	(0.21)	(0.24)	(0.47)	(0.10)	(0.19)
Loan loss reserves/nonperforming assets	1080.85	870.10	513.54	685.65	108.17
*Nine months ended September 30. Note: Assets and revenue are on adjusted basis. Loans include acceptance. All ratios are on an annualized basis. Nonperforming assets include nonperforming loans over three months, restructured loans, foreclosed property, and other substandard assets.					

Analytic services provided by Taiwan Ratings Corporation (TRC) are the result of separate activities designed to preserve the independence and objectivity of ratings opinions. The credit ratings and observations contained herein are solely statements of opinion and not statements of fact or recommendations to purchase, hold, or sell any securities or make any other investment decisions. Accordingly, any user of the information contained herein should not rely on any credit rating or other opinion contained herein in making any investment decision. Ratings are based on information received by TRC. TRC has established policies and procedures to maintain the confidentiality of non-public information received during the ratings process.