

Yuanta Securities Co. Ltd.

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| 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:

- Very good capitalization relative to its risk profile
- Clear market leader in Taiwan's securities industry
- Good business diversification compared with its local peers'

Weaknesses:

- The sensitivity of its market risk exposure to volatile stock market conditions
- Obstacles to further strengthen its funding profile

Rationale

The ratings on Yuanta Securities Co. Ltd. reflect the company's very good capitalization, clear market leadership in Taiwan's securities industry, and good business diversification compared with its local peers'. Counterbalancing factors include the company's market risk exposure which is sensitive to volatile stock market conditions, and the difficulties the company faces to further enhance its funding profile to a strong level due to the wholesale funding nature of the securities business.

Yuanta Securities is the core entity of the Yuanta Financial Holding Co. Ltd. (Yuanta FHC; twA+/Positive/twA-1) group by contribution of capital, profit, and business resources. At the end of September 2010, Yuanta Securities commanded 52% of the group's consolidated capital, followed by Yuanta Securities Finance Co. Ltd. (Yuanta SFC; twAA-/Positive/twA-1+, 28%), and Yuanta Commercial Bank (Yuanta Bank; twAA-/Positive/twA-1+, 22%).

Yuanta Securities' capitalization is very good relative to its risk profile. At the end of September 2010, the company had Taiwan dollar (NT\$) 58 billion in shareholders equity. The company's leverage was 1.4x at the same date, and we estimate its leverage to have increased to about 2.1x at the end of 2010 following the transfer of NT\$51 billion in margin-lending business from its affiliate Yuanta SFC. This acts as a good buffer for the volatile nature of the local securities business.

Yuanta Securities is Taiwan's leading securities house, with a balanced business structure and strong competitive positions in various business segments. At the end of September 2010, the company had a leading 11% share of the island's stock brokerage market. It also has leading positions in other various securities business, particularly financial advisory, derivatives, and underwriting businesses.

We expect Yuanta Securities to continue to pursue business diversification, which is relatively good by local standards. Along with its ongoing efforts to strengthen its business position and diversification in the domestic and overseas markets, Yuanta Securities is likely to develop a more balanced business mix and less reliance on the performance of Taiwan's stock market in the next two to three years, under the emerging benefits of domestic market deregulation.

Yuanta Securities' market risk exposure is sensitive to market conditions. The company's investments in equities and corporate bonds accounted for about 30% of its capital in the 21 months ending September 2010.

Yuanta Securities faces obstacles to further enhance its funding profile to a strong level, due to the wholesale funding nature of the securities business. Since it restarted its margin lending business in October 2010, Yuanta Securities funded 47% of its assets through its own capital, 12% by repurchase agreements, 13% by bank loans/commercial papers, and 27% by other liabilities based on preliminary financial results at the end of 2010.

Enterprise Risk Management

Yuanta Securities has an adequate enterprise risk management (ERM) framework, backed by its proactive management and good risk management tools. Although the company is exposed to considerable market risk due to local market volatility and the nature of the securities business, its ERM has adequate risk management capacity and good risk disciplines. This can be seen in the company's satisfactory profitability track record amid severe market tests. The company's ongoing development of applying the concept of risk-adjusted return on capital into annual budget setting and business line performance measurement is an advanced practice by local standards. This will be beneficial to further enhance and support the company's overall strategic risk management over the long term.

Outlook

The positive outlook reflects our expectation that Yuanta Securities' overall credit profile could improve following the improvement in its earnings profile, for the coming one to two years. The outlook also reflects our view that the company's very good capitalization and its good risk management will serve as a good buffer on the high market risk exposure it faces. The ratings on Yuanta Securities are likely to move in line with the Yuanta FHC group's credit profile. In addition, we expect the group to remain securities-centric for the next one to two years despite its banking subsidiary's above-average growth. In our view, Yuanta FHC and Yuanta Securities are likely to follow prudent business strategies and financial policies in pursuing organic growth as well as through M&A activity.

We may raise the ratings on Yuanta Securities if its 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 the company's 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.

Related Criteria And Research

- [Outlook On Yuanta Financial Holding Co. Ltd. And Key Subsidiaries Revised To Positive On Resilient Earnings Profiles; Ratings Affirmed](#), published on www.taiwanratings.com 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 Co. Ltd. Financial Statistics | | | | | |
|--|----------------------------|---------|---------|----------|---------|
| | --Year ended December 31-- | | | | |
| (Mil. NT\$) | 2010* | 2009 | 2008 | 2007 | 2006 |
| Income statement | | | | | |
| Adjusted revenue | 10,016 | 14,577 | 14,152 | 17,999 | 3,853 |
| % change | (8.61) | 3.00 | (21.37) | 367.12 | 117.11 |
| Pretax profit | 3,440 | 5,954 | 6,076 | 9,183 | 949 |
| % change | (23.15) | (2.01) | (33.83) | 867.12 | 194.38 |
| Net profit | 3,102 | 4,861 | 5,284 | 8,601 | 685 |
| % change | (15.14) | (8.00) | (38.56) | 1,155.55 | 158.19 |
| Composition of adjusted revenue (%) | | | | | |
| Fees and commissions | 65.61 | 66.72 | 55.79 | 56.20 | 64.48 |
| Net trading gains | 6.55 | 13.72 | 8.58 | 10.67 | 9.09 |
| Revenues from warrants | 5.61 | (1.50) | 2.64 | 4.55 | 8.24 |
| Net interest revenues | 4.52 | 4.10 | 3.70 | 5.64 | 2.26 |
| Other revenues | 17.71 | 16.96 | 29.29 | 22.95 | 15.93 |
| Balance sheet | | | | | |
| Total assets | 83,808 | 84,572 | 96,337 | 104,699 | 26,023 |
| % change | (0.90) | (12.21) | (7.99) | 302.33 | (12.05) |
| Adjusted assets | 82,358 | 83,629 | 92,983 | 83,754 | 21,020 |
| % change | (1.52) | (10.06) | 11.02 | 298.45 | (14.07) |
| Total equity | 58,359 | 55,560 | 53,671 | 64,637 | 11,126 |
| % change | 5.04 | 3.52 | (16.96) | 480.96 | 24.33 |
| Profitability (%) | | | | | |
| Pretax income / adjusted revenues | 34.35 | 40.85 | 42.93 | 51.02 | 24.64 |
| Pretax return on average equity | 8.03 | 10.90 | 10.27 | 24.24 | 9.46 |
| After-tax return on average equity | 7.24 | 8.90 | 8.93 | 22.70 | 6.82 |
| Pretax return on average assets | 5.43 | 6.58 | 6.04 | 14.05 | 3.41 |
| After-tax return on average assets | 4.90 | 5.37 | 5.26 | 13.16 | 2.46 |
| Leverage (x) | | | | | |
| Assets / total equity | 1.44 | 1.52 | 1.79 | 1.62 | 2.34 |
| Adjusted assets / total equity | 1.41 | 1.51 | 1.73 | 1.30 | 1.89 |
| *Nine months ended September 30. Note: Yuanta Securities Co. Ltd. (formerly Fuhwa Securities Co. Ltd.) merged with Yuanta Core Pacific Securities Co. Ltd. in September 2007. All data are on an annualized basis. | | | | | |

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