

Management Discussion and Analysis For the year ended December 31, 2016

(This report discusses principal changes in the unaudited consolidated financial statement for the year ended December 31, 2016)

Movement of Money Market and Capital Market

In 2016, the domestic economy resumed recovery momentum following the government stimulus measures, the expansion in tourism sector and the improvement in private consumption. Export sector showed sign of recovery during the second half of 2016. However, Thai economy still remained volatile from both internal and external factors. Therefore, the domestic car sale in the first 11 months of 2016 declined by 2.3% (YoY), totaled 681,930 units. Furthermore, the external economic factors have caused the uncertainty toward global economy, including the U.S. Federal Reserve raising interest rates, the stagnant growth in Eurozone and the economic slowdown in China. The headline inflation for the year 2016 was reported at 0.2%, following the increase in oil prices.

The Bank of Thailand (BOT) maintained the policy rate at 1.50%. The average 3-month fixed deposit rates of Top-4 commercial banks decreased from 1.01% to 0.93% (YoY), while the average minimum lending rate of Top-4 commercial banks decreased from 6.51% to 6.26% (YoY).

The capital market in 2016 improved significantly from the previous year with SET index closed at 1,542.94 points, increased by 254.92 points or 19.8% from the end of 2015. The growth was resulted from the increasing foreign capital inflow, and also the market trading volume has increased from the volatile domestic and global market conditions. Therefore, the average daily turnover increased from 41,141.45 million baht in 2015 to 50,244.97 million baht. .

Major Events

On December 22, 2016, TISCO Bank Public Company Limited and All-Ways Company Limited, the subsidiaries which the Company holds 99.99% and 100% of shares respectively, have an agreement to transfer retail banking business from Standard Chartered Bank (Thai) Public Company Limited. TISCO Bank Public Company Limited will be the transferee of personal lending business, mortgage business, retail banking business, wealth management and individual deposits business while All-Ways Company Limited will be the transferee of credit card business. This transfer aimed to strengthen retail banking business and increase business opportunity to expand customer base from the increasing product offering, as well as the increase benefit value from the transfer. Hereby, the net asset value of the acquired business comprises of total assets and liabilities on the transfer date. As of 30 September 2016, the net asset value was approximately 5,500 million baht, which consisted of approximate total assets of 41,600 million baht and total liabilities of 36,100 million baht. The transfer is expected to be completed within the year 2017 after the approval from the Bank of Thailand and shareholders of the transferor and transferee.

Operating Results

The Management Discussion and Analysis compares operating performance of the year 2016 and 2015

TISCO Financial Group Public Company Limited ("the Company") had net profit from operations on a standalone basis totaling 3,118.93 million baht, mainly contributed by service fee income from subsidiary companies within the group. As a holding company, TISCO Financial Group Public Company Limited operates as shareholder in other company and no other major business. Therefore, the analysis was based on the Company's consolidated operating performance and financial position which comprised of 2 main businesses: commercial banking business and securities business.

In 2016, the net profit attributed to owners of the Company totaled 5,005.40 million baht, increased by 755.28 million baht (17.8% YoY), which mainly contributed by improved net interest income and non-interest income from core business¹, as well as the lower provision expense comparing to the previous year. Net interest income increased by 7.8% (YoY) from the ability to maintain overall loan yield and the effective cost management. Non-interest income from core business improved by 1.6% (YoY), mainly resulting from the increase in brokerage fee income by 2.8% (YoY) following increasing market trading volume. Banking fee increased by 0.9% (YoY) owing to the improvement in bancassurance business. Moreover, the Company recorded investment banking fee from underwriting service during the past year. Meanwhile, asset management fee remained stable comparing to the previous year. Moreover, provision expense declined by 24.7% (YoY) from the improved asset quality. All in all, the provision remained at a cautious level, partly from the setup of general provision against business volatility amid the economic uncertainty.

Non-performing loans (NPLs) continually declined following improved asset quality in both hire purchase business and corporate lending business, thanks to effective credit control. In addition, the Company reclassified Sahaviriya Steel Industries Pcl. (SSI) from non-performing loan to special mention loan after the Central Bankruptcy Court approved the debt rehabilitation plan. As a result, the NPL ratio at the end of 2016 decreased from 3.23% to 2.54% (YoY) while the loan loss provision coverage ratio increased to 139.8%.

Basic earnings per share for the year 2016 was at 6.25 baht per share, increased from 5.31 baht per share in 2015. Meanwhile, the return on average equity (ROAE) was at 16.9%, increased from 15.8% (YoY).

Net Interest Income

Net interest income in 2016 was 10,920.43 million baht, increased by 790.58 million baht (7.8% YoY). Total interest income was 16,011.54 million baht, decreased by 876.01 million baht (5.2% YoY) while interest expense declined by 1,666.59 million baht (24.7% YoY) to 5,091.11 million baht, owing to a further decline in cost of fund and the Company's effective cost management.

¹ Non-interest income from core business was net of promotion expenses relating to the hire purchase business.

Yield on loan improved from 6.5% to 6.6% (YoY) from the shift in loan portfolio mix from hire purchase loan to consumer loans that offer higher yield. While, cost of fund decreased from 2.6% to 2.2% (YoY) driven by a continual decline in funding cost. Consequently, loan spread increased from 3.9% to 4.5% (YoY). In addition, the net interest margin also rose from 3.4% to 4.0% (YoY).

The Company reported net interest income after impairment loss of loans and debt securities totaled 6,948.07 million baht, increased by 2,095.63 million baht (43.2% YoY). Impairment losses on loans totaled 3,972.37 million baht, comparing with 5,277.42 million baht in 2015, mainly resulting from the effective credit control.

Non-interest Income

Non-interest income of the Company's core businesses reported at 5,932.70 million baht, increased by 93.75 million baht (1.6% YoY), mainly due to the increase in brokerage fee income by 22.58 million baht (2.8% YoY) to 825.27 million baht following increasing market trading volume. Banking fee income was reported at 3,778.97 million baht, increased by 35.25 million baht (0.9% YoY) from the improvement in bancassurance business. Moreover, the Company recorded the investment banking fee amounting 70.76 million baht from underwriting service during the year. Nonetheless, asset management fee was at 1,141.36 million baht, remained stable comparing to the previous year.

Non-interest Expenses

Non-interest expenses were 6,541.03 million baht, increased by 1,014.01 million baht (18.3% YoY), mainly from the increase in variable expenses associated with revenue growth. The Company still maintained effective operating cost control, resulting in low cost to income ratio at 39.0%.

Corporate Income Tax

In 2016, the corporate income tax was 1,220.90 million baht, equivalent to the effective tax rate of 19.6%, which remained at the same level as in 2015.

Financial Position

The Management Discussion and Analysis on operating results on financial status is a comparison between the financial positions as of December 31, 2016 and December 31, 2015

Assets

As of December 31, 2016, the Company's total assets were 271,279.65 million baht, decreased by 3.2% (YoY) mainly due to the decline in loan portfolio from 238,259.84 million baht to 224,934.00 million baht (5.6% YoY) and the decrease in investments from 8,332.42 million baht to 7,188.84 million baht (13.7% YoY).

Liabilities

As of December 31, 2016, total liabilities were 239,984.23 million baht, decreased by 4.8% (YoY), due to the decrease in total deposits from 165,281.11 million baht to 161,034.44 million baht (2.6% YoY), the decrease in interbank and money market from 10,030.06 million baht to 5,196.60 million baht (48.2% YoY) and the decline in debentures from 67,582.00 million baht to 64,362.00 million baht (4.8% YoY). The liabilities mix comprised of 67.1% total deposits including bill of exchange, 2.2% interbank and money market items, 26.8% debentures, and 3.9% other liabilities.

Shareholders' Equity

As of December 31, 2016, shareholders' equity was 31,295.41 million baht, increased by 3,101.09 million baht (11.0% YoY) from an increase in retained earnings of the year 2016. As a result, the book value per share (BVPS) as of December 31, 2016 was 39.09 baht per share, increased from 35.21 baht per share (YoY).

Business Segment Performance

(1) Banking Business

Loans

Total loans and receivables as of December 31, 2016 were 224,934.00 million baht, declined by 13,325.83 million baht (5.6% YoY), following weak domestic economy and the slow recovery in domestic auto market. The composition of loan portfolio was 71.8% of retail loans, 20.7% of corporate loans, 7.3% of commercial loans and 0.2% of other loans.

Retail Lending portfolio totaled 161,492.31 million baht or decreased by 7.5% (YoY), where the portfolio consisted of 85.0% car and motorcycle hire purchase, 14.4% consumer loans and 0.6% mortgage loans. The outstanding hire purchase loans totaled 137,285.30 million baht, declined by 10.2% (YoY), resulting from the weak domestic consumption and high level of household debt. The domestic car sale in the first 11 months of 2016 was 681,930 units, decreased by 2.3% (YoY), compared to 698,168 units in the first 11 months of 2015. The car penetration rate of TISCO for the first 11 months declined from 8.8% to 8.1% (YoY). Meanwhile, consumer loans amounted 23,228.20 million baht, increased by 2,828.97 million baht (13.9% YoY).

Corporate Lending portfolio totaled 46,509.94 million baht, increased by 3,182.64 million baht (7.3% YoY), mainly due to the loan drawdown from the clients in public utilities and services sector.

Commercial Lending portfolio totaled 16,454.07 million baht, dropped by 3,434.54 million baht (17.3% YoY) primarily from the decline in loan demand in logistic sector and Car Inventory Financing.

Other Loans portfolio totaled 477.68 million baht, decreased by 34.70 million baht (6.8% YoY).

Deposits and Borrowings

Total deposits and borrowings totaled 225,396.44 million baht, decreased by 3.2% (YoY). Total deposits totaled 161,034.44 million baht, decreased by 4,246.67 million baht (2.6% YoY), while debentures totaled 64,362.00 million baht, decreased by 3,220.00 million baht (4.8% YoY). As of December 31, 2016, the Bank had liquid assets totaling 40,765.98 million baht or 18.1% of total deposits and borrowings.

Non-Performing Loans (NPLs) and Loan Loss Provision

In 2016, the NPL ratio was reported at 2.54%, decreased from 3.23% (YoY). NPL ratio of retail loan, corporate loan, and commercial loan were 2.91%, 0.89%, and 3.62% respectively. Total NPLs reported at 5,710.14 million baht, decreased by 1,990.69 million baht (25.9% YoY), which comprised of 5,120.99 million baht from the Bank and 589.15 million baht from other subsidiaries. The NPL amount continually declined (YoY) driven by the improved credit quality of the core loan portfolio, which consists of hire purchase loan and corporate loan, together with the NPL of commercial loan that reverted back to normal, following the effective credit control. Furthermore, at the end of 2016, the Company reclassified Sahaviriya Steel Industries Pcl. (SSI) from non-performing loan to special mention loan after the Central Bankruptcy Court approved the debt rehabilitation plan.

The Company set up provision for the year at 3,972.37 million baht, accounted for 1.72% of average loan, and decreased comparing with 5,277.42 million baht (YoY), mainly due to the improved asset quality of the loan portfolio. Generally, the provision still remained at a caution level amidst the environment of high economic uncertainty. The provision included the setup of excess loan loss reserve of 1,942 million baht from the previous year, to cushion against potential business volatility. Hence, if excluded the setup of excess reserve, the provision would report at 0.88% of average loan. As of the year 2016, loan loss reserve of the Company was 7,983.64 million baht while total loan loss reserve of the Bank was 7,500.53 million baht which was higher than the minimum loan loss reserve required by the Bank of Thailand at 4,345.32 million baht or accounted 172.61% of minimum loan loss reserve requirement. The loan loss provision coverage ratio at the end of 2016 increased to 139.8%.

(2) Securities Business

In 2016, average daily turnover of TISCO Securities was 2,152.29 million baht, increased by 1.9% (YoY) from 2,112.53 million baht, following an increase in market trading volume during the capital market volatility. In addition, TISCO Securities reported brokerage fee income growth of 2.8% (YoY) totaled 825.27 million baht. Nonetheless, TISCO Securities' market share declined from 2.8% to 2.4% (YoY). The market share of retail investors decreased from 1.9% to 1.6% (YoY), while the market share of local institution sector (excluding proprietary trading) declined from 7.0% to 6.1% (YoY). Moreover, the market share of foreign institution sector decreased from 3.3% to 2.5% (YoY). All in all, TISCO brokerage volume comprised of 30.0% of local institutions, 30.7% of foreign institutions, and 39.3% of retail customers.

(3) Asset Management Business

As of December 31, 2016, assets under management of TISCO Asset Management Co., Ltd. was reported at 193,162.42 million baht, increased by 8.2% (YoY), mainly from the growth in all business areas. The fee income from asset management in 2016 totaled 1,141.36 million baht, remained stable comparing to the previous year. Throughout the year 2016, TISCO Asset Management Co., Ltd. continuously issued various types of mutual funds corresponding to market demands, namely Equity Trigger funds and Foreign Investment Fund (FIF) including fixed income funds and equity funds.

The composition of total asset under management was 67.9% provident fund, 13.8% private fund, and 18.3% mutual fund. Total market share of TISCO Asset Management Co., Ltd. as of November 30, 2016 was 3.1%, ranking 10th in the market. The market share of provident fund was 13.4%, ranking 3rd in the market. The market share of private fund was 3.5%, ranking 8th in the market. For mutual fund, the market share was 0.8%, ranking 16th in the market.

Risk Management

As of December 31, 2016, TISCO Group's internal capital stood at 28,817.88 million baht comprising of Tier-I capital and available reserve adjustment. The integrated risk capital increased by 450.16 million baht from the end of 2015 to 10,268.02 million baht, mainly resulting from an increase in credit risk capital. In addition, the capital surplus remained strong at 18,549.86 million baht or 64.4% of total capital.

Comparing to the end of year 2015, the credit risk capital stood at 7,721.47 million baht, which increased by 686.55 million baht or 9.8% following some conservative adjustment in risk capital buffer, while loan portfolio contracted by 5.6% during the year. The non-performing loan of TISCO Group decreased from 3.2% to 2.5% compared to the end of 2015.

The market risk capital decreased from 495.33 million baht to 204.62 million baht, resulting from a decrease in risk capital of investment portfolio. Meanwhile, the overall duration gap decreased to 0.78 year, which was in a manageable level. The assets duration increased from 1.47 year to 1.48 year, while the liabilities duration excluding saving and current accounts, which are less sensitive to the interest rate movement, rose from 0.56 year to 0.70 year.

In terms of regulatory capital requirement of the Bank and Securities Company, the positions were strong and sufficient levels to cushion for the expansion of asset in the future. At the end of December 2016, the projected regulatory capital adequacy ratio based on IRB approach (BIS ratio) of the bank stood at 19.78%, remaining higher than the 9.125% required by the Bank of Thailand. Tier-I and Tier-II capital adequacy ratio stood at 14.89% and 4.89%, respectively, in which Tier-I capital adequacy ratio also remained higher than the minimum requirement at 6.625%. Meanwhile, the net capital rule (NCR) of TISCO Securities Co., Ltd. stood at 85.73%, which was higher than the minimum required ratio by the SEC of 7.0%.

Table 1: Consolidated Revenue Structure

Type of Revenue	2015		2016		Change % YoY
	Amount (Bt. million)	%	Amount (Bt. million)	%	
Interest income					
Interest on loans	5,681.85	35.3	5,568.41	33.2	(2.0)
Interest on interbank and money market items	540.42	3.4	497.30	3.0	(8.0)
Hire purchase and financial lease income	10,409.47	64.7	9,749.53	58.2	(6.3)
Investments	255.82	1.6	196.31	1.2	(23.3)
Total interest income	16,887.55	104.9	16,011.54	95.5	(5.2)
Interest expenses	(6,757.70)	(42.0)	(5,091.11)	(30.4)	(24.7)
Net interest income	10,129.86	62.9	10,920.43	65.2	7.8
Fee income					
Fee income	5,255.97	32.7	5,396.85	32.2	2.7
Fee expenses	(198.93)	(1.2)	(230.08)	(1.4)	15.7
Net fee income	5,057.03	31.4	5,166.77	30.8	2.2
Gain on investment and foreign exchange transaction	225.10	1.4	3.13	0.0	(98.6)
Share of profit from invest in subsidiaries	97.66	0.6	131.21	0.8	34.4
Other operating income	979.28	6.1	838.77	5.0	(14.3)
Total operating income	16,488.93	102.5	17,060.31	101.8	3.5
Expenses to business promotion relating to the business	(396.30)	(2.5)	(302.92)	(1.8)	
Total net operating income	16,092.62	100.0	16,757.39	100.0	4.1
Other operating expenses	(5,527.02)		(6,541.03)		
Bad debt and doubtful account and impairment loss of debt securities	(5,277.42)		(3,972.37)		
Profit before income tax and minority interest	5,288.19		6,243.99		18.1
Corporate income tax expenses	(1,032.46)		(1,220.90)		
Profit before minority interest	4,255.72		5,023.09		18.0
Non-controlling interests of the subsidiaries	(5.60)		(17.69)		
Net profit	4,250.12		5,005.40		17.8

Table2: Interest Spread

%	2015	2016
Yield on Loans	6.5	6.6
Cost of fund	2.6	2.2
Loan spread	3.9	4.5

Table 3: Assets Breakdown

Assets	December 31, 2015		December 31, 2016		% Change
	Amount (Bt. million)	%	Amount (Bt. million)	%	
Cash	1,101.29	0.4	1,149.00	0.4	4.3
Interbank and Money Market Items	31,162.64	11.1	38,067.42	14.0	22.2
Derivative Asset	0.00	0.0	0.00	0.0	n.a.
Investment in Fixed income	6,998.30	2.5	5,785.79	2.1	(17.3)
Investment in Equity	1,334.14	0.5	1,403.07	0.5	5.2
Investments in subsidiaries, associate and joint venture	284.11	0.1	442.75	0.2	55.8
Corporate Loans	43,327.30	15.5	46,509.94	17.1	7.3
Retail Loans	174,531.55	62.3	161,492.31	59.5	(7.5)
Commercial Loans	19,888.60	7.1	16,454.07	6.1	(17.3)
Other Loans	512.38	0.2	477.68	0.2	(6.8)
Allowance for doubtful accounts and for loss on debt restructuring	(6,168.27)	(2.2)	(7,983.64)	(2.9)	29.4
Other Assets	7,321.65	2.6	7,481.26	2.8	2.2
Total – The Company	280,293.68	100.0	271,279.65	100.0	(3.2)

Table 4: Loans and Receivables Breakdown

Type of Business	December 31, 2015		December 31, 2016		% Change
	Amount	%	Amount	%	
	(Bt. million)		(Bt. million)		
Manufacturing and commerce	12,126.50	5.1	10,496.69	4.7	(13.4)
Real estate and construction	11,987.70	5.0	11,696.34	5.2	(2.4)
Public utilities and services	18,837.43	7.9	23,908.50	10.6	26.9
Agriculture and mining	375.67	0.2	408.41	0.2	8.7
Corporate Loans	43,327.30	18.2	46,509.94	20.7	7.3
Commercial Loans	19,888.60	8.3	16,454.07	7.3	(17.3)
Hire purchase	152,907.78	64.2	137,285.30	61.0	(10.2)
Mortgage	1,224.55	0.5	978.81	0.4	(20.1)
Consumer	20,399.23	8.6	23,228.20	10.3	13.9
Retail Loans	174,531.55	73.3	161,492.31	71.8	(7.5)
Others	512.38	0.2	477.68	0.2	(6.8)
Total – The Company	238,259.84	100.0	224,934.00	100.0	(5.6)

Table 5: NPL Breakdown by Area

Type of Business	December 31, 2015			December 31, 2016			% Change
	% NPL	Amount (Bt. million)	%	% NPL	Amount (Bt. million)	%	
Manufacturing and commerce	8.08	979.54	12.7	1.78	187.21	3.3	(80.9)
Real estate and construction	0.79	94.42	1.2	0.70	81.57	1.4	(13.6)
Public utilities and services	0.57	107.26	1.4	0.52	123.39	2.2	15.0
Agriculture and mining	2.09	7.86	0.1	4.85	19.83	0.3	152.3
Total NPL - Corporate Loans	2.74	1,189.08	15.4	0.89	412.01	7.2	(65.4)
NPL-Commercial Loans	2.03	404.66	5.3	3.62	595.16	10.4	47.1
Hire purchase	3.53	5,403.58	70.2	2.94	4,042.75	70.8	(25.2)
Mortgage	6.67	81.62	1.1	9.32	91.24	1.6	11.8
Consumer	3.04	619.51	8.0	2.44	567.17	9.9	(8.4)
Total NPL - Retail Loans	3.50	6,104.71	79.3	2.91	4,701.16	82.3	(23.0)
Others	0.46	2.38	0.0	0.38	1.81	0.0	(24.0)
Total NPL – The Company	3.23	7,700.83	100.0	2.54	5,710.14	100.0	(25.9)

Table 6: Liabilities Breakdown by Area

Type of Borrowings	December 31, 2015		December 31, 2016		% Change
	Amount (Bt. million)	%	Amount (Bt. million)	%	
Deposits	165,281.11	65.6	161,034.44	67.1	(2.6)
Interbank and money market items	10,030.06	4.0	5,196.60	2.2	(48.2)
Debentures	67,582.00	26.8	64,362.00	26.8	(4.8)
Others	9,206.18	3.7	9,391.19	3.9	2.0
Total – The Company and Subsidiaries	252,099.35	100.0	239,984.23	100.0	(4.8)

Table 7: Deposits Structure

Type of Deposits	December 31, 2015		December 31, 2016		% Change
	Amount (Bt. million)	%	Amount (Bt. million)	%	
Current accounts	3,122.04	1.9	3,690.70	2.3	18.2
Saving accounts	48,272.47	29.2	51,928.03	32.2	7.6
Fixed accounts	17,734.17	10.7	14,839.89	9.2	(16.3)
Negotiate certificate deposit	89,215.51	54.0	84,608.90	52.5	(5.2)
Short-term borrowings	6,936.92	4.2	5,966.92	3.7	(14.0)
Total deposits	165,281.11	100.0	161,034.44	100.0	(2.6)

Table 8: Assets under Management Breakdown by Type of Fund

Type of Fund	December 31, 2015		December 31, 2016		% Change
	Amount	%	Amount	%	
	(Bt. million)		(Bt. million)		
Provident Fund	118,736.97	66.5	131,073.24	67.9	10.4
Private Fund	26,413.25	14.8	26,732.95	13.8	1.2
Mutual Fund	33,404.36	18.7	35,356.24	18.3	5.8
Total	178,554.58	100.0	193,162.42	100.0	8.2

Table 9: Average Duration Mismatch of Assets and Liabilities and Its Impact

Type of Fund	Duration (years)		1-Y Net interest income change to 1% interest rate increase (MB)	
	December 31, 2015	December 31, 2016	December 31, 2015	December 31, 2016
	Assets	1.47	1.48	1,035.44
Liabilities*	0.56	0.70	(1,323.43)	(1,065.21)
Net Gap	0.91	0.78	(287.99)	10.29

Note: * Exclude saving and current account