FitchRatings

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Fitch Revises Outlook on Capital Securities Corporation to Stable; Affirms at 'BBB-'

Fitch Ratings - Hong Kong - 26 Nov 2020: Fitch Ratings has revised the Outlook on Taiwan-based Capital Securities Corporation's Long-Term Issuer Default Rating (IDR) of 'BBB-' and National Long-Term Rating of 'A(twn)' to Stable from Negative and affirmed the ratings. Fitch has also affirmed the National Short-Term Rating of 'F1(twn)'.

The Outlook revision reflects Fitch's view that Capital Securities will maintain its credit profile in 2020 and 2021 as it has shown it has been able to absorb the negative impact of the coronavirus outbreak to date and it stands to benefit from the post-pandemic stabilisation in Asia's economy. Stock-market activities in Taiwan have recovered faster than expected since 1Q20, contributing to resilience in Capital Securities' operating performance and financial strength since the outbreak of the coronavirus.

Capital Securities is the largest independent full-service securities firm in Taiwan, with a market share of 4% in the domestic brokerage business. Its ranking and market share in retail brokerage have been steady since 2015. It also has strong market positions in fixed-income underwriting and warrant issuance.

Key Rating Drivers

Capital Securities' ratings are driven by its longstanding and stable franchise in Taiwan's stockbroking sector, and sound capital profile. The ratings are constrained by the company's limited diversity, which could lead to volatile earnings. Its major income source, brokerage, is vulnerable to weak market sentiment, while income from trading and underwriting is inherently more volatile and subject to market risk.

Capital Securities has maintained a sound capital profile. Its Fitch-defined net adjusted leverage ratio rose to 4.7x by end-June 2020 and has ranged between 3.2x and 4.7x from 2015 to June 2020.

Capital Securities' investment portfolio comprises large exposure to government and investment-grade private-sector bonds and a diversified stock portfolio. The closer correlation between asset classes at the height of the COVID-19 pandemic resulted in impairment losses to its investment portfolio in 1Q20, but the losses were offset by a strong rebound in trading income in 2Q20 and 3Q20. While the company's risk management system has been able to govern its risk-taking in trading and securities financing as well as operational risks, the results in 1Q20 exposed the company's vulnerability to extreme market conditions.

RATING SENSITIVITIES

Factors that could, individually or collectively, lead to positive rating action/upgrade:

Sustained improvement in business diversity and earnings quality would be positive for the ratings. A strengthening in its market position in stock brokerage to that comparable with the top three players and an associated improvement in operating profit/equity to above 10% for a sustained period would also be positive for the ratings.

Factors that could, individually or collectively, lead to negative rating action/downgrade:

Capital Securities' ratings would face pressure if the pursuit of business expansion and profitability undermined its capital and funding and liquidity profiles, such that the net adjusted leverage ratio is above 5x for a sustained period.

The ratings are also sensitive to an increased appetite for risk, in particular, higher balance-sheet exposure to market risk or greater revenue sensitivity from trading activities. A failure of the company's risk-management system to contain market risk would also be credit negative.

Best/Worst Case Rating Scenario

International scale credit ratings of Financial Institutions and Covered Bond issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of four notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit [https://www.fitchratings.com/site/re/10111579]

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG Considerations

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg

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Rating Actions

ENTITY/DEBT	RATING			RECOVERY	PRIOR
Capital Securities Corporation	LT IDR	BBB-	Affirmed		BBB-
	Natl LT	A(twn)	Affirmed		A(twn)
	Natl ST	F1(twn)	Affirmed		F1(twn)

RATINGS KEY OUTLOOK WATCH

RATINGS KEY	OUTLOOK	WATCH
POSITIVE	⊕	◆
NEGATIVE	⊖	◆
EVOLVING	◎	◆
STABLE	◎	

Applicable Criteria

National Scale Rating Criteria (pub.08 Jun 2020)

Non-Bank Financial Institutions Rating Criteria (pub.28 Feb 2020) (including rating assumption sensitivity)

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Endorsement Status

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