PhilRatings
PHILIPPINE RATING SERVICES CORPORATION

RATING REPORT
PHILIPPINE SAVINGS BANK

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Rationale

The assigned issuer credit rating of ***PRS Aaa (corp.)***for Philippine Savings Bank (PSBank) takes into consideration the following rating factors:

- PSBank's well-defined growth strategy, anchored on the bank's solid understanding of its market;
- Positive revenue growth going forward, supported by increasing interest income from the bank's continuous loan portfolio expansion;
- Expectations that PSBank's funding profile will continue to improve, backed by the growth in current and savings deposits; and
- The favorable outlook for domestic consumer credit.

PSBank is a strong player in the consumer credit market, which accounts for approximately 80% of its loan portfolio. The bank has been following a more stable growth strategy, following years of aggressive expansion aimed at strengthening market recognition of the PSBank brand. The consumers, however, remain as the bank's target market, and will continue to dictate the bank's strategy going forward. Focus will remain on the needs and wants of the consumer market, and responding to these needs and wants with innovations that will make PSBank stand out from among its peers.

While the addition of brick-and-mortar branches will continue to support PSBank's expanding market reach, information technology is seen to play an increasing role in the bank's competitive strategy, as part of efforts to provide a better response against other players to its customers' evolving needs and wants.

Interest income, a more stable and recurring revenue source, continued to post increases in 2014 and 2015, as well as in the first quarter of 2016 (1Q2016), attributable to the expansion of the bank's loan portfolio. The increases helped counterbalance the impact of more volatile non-interest revenues (particularly, trading gains) on PSBank's topline. While forecasts show a recovery in non-interest income, core interest income will continue to account for more than 70.0% of revenues, as the bank builds up its loan portfolio in response to continued demand for consumer credit.

While time deposits continue to account for the bulk of PSBank's deposits, its rate of increase has been slower compared with the growth of the bank's current and savings accounts (CASA). Also, it is noted that the growth of CASA between 2014 and March 2016 was at 28.8%. These developments are seen to enhance PSBank's funding profile, as CASA is viewed as more stable and less expensive than time deposits.

CASA is expected to grow by around 20% by end 2016, underpinned by the bank's continued branch expansion (and consequently, increasing awareness of the PSBank brand) and incentive programs.

Since 2008, consumer loans (CLs) of the domestic banking industry have been posting annual increases. Consumer lending continued to expand, as the Philippine economy sustained its growth amid the steady increase in overseas Filipino (OF) remittances, a growing Business Process Outsourcing (BPO) industry, the solid performance of the services sector, and heightened consumer spending and lending. More Filipinos, particularly the growing middle class, continued to invest in their first properties and cars, as developers and retailers made available a wide array of property and car models.

The Philippine banking industry's loans for consumer purchases and credit card use substantially went up by 17.5% in 2015, to break through the P1.0 trillion-mark for the first time. Universal banks (unibanks), commercial banks (KBs) and thrift banks (TBs) reported P1.061 trillion in consumer loans, as of end-2015. TBs' consumer loans jumped by 25.4% to P414.4 billion, way ahead of the 13.0% hike in the lending of unibanks and KBs.

Consumer lending in the Philippines is expected to continue its growth at double-digit rates, because of the projected improvement in the country's economy. Increasing disposable incomes will encourage more investments in areas such as durable goods, education, houses, personal transportation and business. Presently, consumer spending accounts for 70.0% of the country's Gross Domestic Product (GDP). Growth in consumer loans will be further fueled by banks' aggressive attitude towards developing and increasing their loan portfolios, as well as accommodating consumers in different socio-economic classes. Among the Association of Southeast Asian Nations (ASEAN) economies, Philippine banks have the lowest exposure to consumer credit, thus indicating that there is still room for growth in this area.

PROFILE

Philippine Savings Bank (PSBank) was the second largest thrift bank in the Philippines with assets of P173.9 billion, based on its published statement of condition, as of March 31, 2016. PSBank's market share of the thrift banking system was approximately 17.2% of assets, 16.4% of loans, and 16.8% of deposits. PSBank is a strong player in the consumer market, which accounts for approximately 80% of its loan portfolio. Other services offered by the bank include deposits, treasury and trust.

PSBank's distribution network consisted of 255 branches and 625 automated teller machines (ATMs), as of March 31, 2016. The figures represented additions of seven branches and eleven ATMs from end-2015. The branches are well dispersed throughout Metro Manila and provincial areas. PSBank's ATM network, on the other hand, consisted of 267 onsite and 358 offsite machines.

As of March 31, 2016, PSBank's asset size of P173.9 billion was bigger compared with some mid-size universal and domestic commercial banks. This observation is notable as universal and commercial banks represent the largest single group, resource-wise, of financial institutions (FIs) in the Philippines. They offer the widest variety of banking services among FIs. In addition to the function of an ordinary commercial bank, unibanks are also authorized to engage in underwriting and other functions of investment houses, and to invest in equities of non-allied undertakings.[1]

OWNERSHIP AND LEGAL STATUS

PSBank is a licensed savings and mortgage bank under Bangko Sentral ng Pilipinas (BSP) regulations. PSBank is considered to have a strong Parent in Metropolitan Bank and Trust Company (Metrobank), which owned seventy-six percent (76.0%) of PSBank, as of report writing date.

Metrobank was the Philippines' second-largest bank with assets of P1.7 trillion, as of March 31, 2016. The bank similarly ranked second based on capital accounts (P195.0 billion), and third in terms of loans (P848.7 billion) and deposits (P1.2 trillion). Metrobank's CAR stood at a very comfortable 17.5%, while asset quality remained sound, taking into account the bank's low non-performing assets (NPA) ratio of less than 1%.[2]

Metrobank bank has always been particularly strong in the middle market corporate sector, a significant portion of which consists of Filipino-Chinese businesses. Metrobank was one of the first domestic banks to be granted a unibank license by the BSP, allowing the bank to engage in "non-allied undertakings" (automobile manufacturing, travel services and real estate), as well as finance-related businesses (insurance, savings and retail banking, credit card services and leasing).

In April 2016, Fitch Ratings (Fitch) affirmed Metrobank's long-term IDR of BBB-. The rating is Fitch's minimum investment grade rating. Fitch stated that Metrobank's rating is supported by the bank's improved asset quality, backed by prudent underwriting standards and controls, adequate capital ratios and stable funding profile.

Metrobank is the banking arm of GT Capital Holdings, Inc. (GTCap), the publicly-listed holding firm of the family of George S.K. Ty. GTCap has diverse investments in companies that are important players in their respective markets (Metrobank, Toyota Motor Philippines Corporation, Federal Land, and Philippine AXA Life Insurance Corporation). As of report writing date, GTCap has an issue rating of PRS Aaa for its outstanding P22.0 billion bonds.

In principle, PhilRatings views concentrated ownership structures less favorably, particularly where ownership and control rests with one individual or a small group of individuals. The Ty family, however, is viewed as a stable and supportive influence to the GTCap Group, given the family's well-established reputation and credibility. Based on their latest audited financial statements, both PSBank and Metrobank were compliant with BSP's conservative regulations regarding lending by banks to directors,

[1]http://www.bsp.gov.ph/banking/bspsup.asp
[2]Source: Business World 1st Quarter Banking Report 2016

owners, shareholders, and other related interests (DOSRI). PSBank is professionally run, with its senior management team comprised of well-experienced officers.

PSBank has been strike-free throughout its entire history. Recently, PSBank and the PSBank Employees Union (PSBEU) successfully concluded its Collective Bargaining Agreement (CBA) for the period January 2016 to December 2018. The Memorandum of Agreement was signed by both parties on December 16, 2015, while the formal signing was done on February 12, 2016.

STRATEGY

PSBank has been following a more stable growth strategy, following years of aggressive expansion aimed at strengthening market recognition of the PSBank brand. Consumers, however, remain as the bank's target market, and will continue to dictate the bank's strategy going forward. Focus will remain on the needs and wants of the consumer market, and responding to these needs and wants with innovations that will make PSBank stand out from among its peers.

While the addition of brick-and-mortar branches will continue to support PSBank's increasing market reach, information technology is seen to play an increasing role in the bank's competitive strategy, as part of efforts to provide a better response against other players to its customers' evolving needs and wants. New products and services introduced in 2015 appear to support this observation.

In June 2015, PSBank launched its ATM Lock and PSBank Mobile App 2.0. The PSBank Mobile 2.0 has a user-friendly interface and a security feature that allows a bank client to do more secure and faster banking transactions, even while he is on the go. The enhanced mobile app allows the client to do more using his mobile phone, such as applying for a loan, searching for an ATM or a branch, transferring funds, paying bills, buying reloads, among others. The ATM Lock, on the other hand, is an innovation that allows a depositor to prevent unauthorized use of his card.

In August 2015, PSBank launched its enhanced website. PSBank's enhanced website now sports a cleaner look and a more streamlined design which allows easy navigation of its features. The adaptive design is suited for any device whether laptop, tablet, or mobile phone.

Also in August 2015, the bank introduced its PSBank Queue Anywhere service. The PSBank Queue Anywhere is an automated lobby management system. The system allows a client to book his transaction ahead with a PSBank branch, thus resulting in less time spent to complete his transaction.

In February 2016, PSBank launched its social media accounts (Facebook, Instagram, Twitter and You Tube). The social media accounts target active netizens who are 25 to 34 years old. In the same month, the bank also introduced the PSBank Online Loan Application (POLA), which allows clients to apply for a car loan via short message service (SMS), and get a credit decision within 24 hours from the time of the loan application. Outlook for POLA is promising given the initial favorable reception of the market to this service.

PSBank's newest service, the PSBank Business Online Buddy (BOB), is an online banking facility particularly designed for commercial or business clients. The PSBank BOB allows clients to: do banking transactions, anytime and anywhere; manage their accounts, monitor cash flows and keep track of receivables and payables; and perform cash management functions (pay suppliers and utilities, transfer funds, and sweep transactions from satellite accounts to mother account). Requirements for the PSBank BOB, which is presently in the pilot testing stage, are basic and easy to comply with as this service mainly caters to the simple cash management requirements of small and medium enterprises (SMEs).

PSBank opened seven new branches in the first four months of 2016, thus ending April 2016 with 255 branches. It had 626 ATMs: 268 onsite and 358 offsite. PSBank will expand its branch network in the next five years, and will continue to install ATMs in non-branch locations.

Reliability of the bank's technology infrastructure will be a priority, to support strategic initiatives on information technology and improve operating efficiency. PSBank will also continue to enhance its online and mobile banking facilities going forward, taking into account the changing preferences of its clients.

Outlook for Consumer Lending[3]

The Philippine banking industry's loans for consumer purchases and credit card use substantially increased by 17.5% in 2015, to breach the P1.0 trillion-mark for the first time. Unibanks, KBs, and TBs reported P1.061 trillion in consumer loans, as of end-2015. TBs' consumer loans significantly went up by 25.4% to P414.4 billion, outpacing the 13.0% hike in the lending of unibanks and KBs.

Since 2008, CLs of the domestic banking industry have been posting yearly increases. Consumer lending continued to expand, as the Philippine economy sustained its growth, amid the steady increase in OF remittances, a growing BPO industry, the solid performance of the services sector, and heightened consumer spending and lending. More Filipinos, particularly the growing middle class, continued to invest in their first properties and cars, as developers and retailers made available a wide array of property and car models.

Increased demand, along with tight competition, encouraged banks to launch various types of promotions to increase their market share. Banks offered enhanced products and services, more flexible payment terms, lower interest rates and giveaways such as free insurance. These promotions were undertaken with the assurance of shorter loan processing time, to prevent prospective clients from backing out or transferring to another lender.

Total motor vehicle loans for the purchase of cars and motorcycles jumped by 32.1% to P303.9 billion. Statistics from the ASEAN Automotive Federation showed that Philippine motor vehicle sales grew by

[3] Sources:
http://www.bsp.gov.ph/publications/media.asp?/id=4053
http://www.euromonitor.com/consumer-lending-in-the-philippines/report
http://www.business.inquirer.net/210072/consumer-loans-breaches-p1-trillion-mark-in-2015#ixzz4BvncF7QO

23.0% to 288,609 units in 2015. The Philippines was the only ASEAN country that posted an annual growth in sales of two-wheel vehicles, with motorcycles and scooters sales posting an 8.0% growth to 850,509 units.

Loans for residential real estate in 2015 went up by 11.5% to P444.0 billion. Going forward, property developers anticipate the high demand in properties will result in the establishment of more housing projects within and outside Metro Manila. Ownership of low-priced homes will likely be driven by first-time homeowners, while the acquisition of mid-priced and high-end properties will come from OFs.

Total card receivables increased by 9.1% to P179.3 billion, boosted by banks' attractive and comprehensive reward programs. Banks' partnership with retailers offered flexible payment schemes and low, if not, zero interest rates that consumers took advantage of, particularly in the purchase of high-priced items such as appliances, furniture and gadgets. Banks also developed credit cards that specifically targeted the growing middle-class. This development is expected to push credit card ownership and transaction value in the coming years.

BSP data showed that the non-performing CLs of the banking industry represented 4.5% of their total CLs as of end-2015, a slight decrease from 4.8% as of end-2014. Banks also provisioned 58.8% of their non-performing CLs as buffer for potential credit losses.

Consumer lending in the Philippines is expected to continue its growth at double-digit rates, due to the projected improvement of the country's economy. Increasing disposable incomes will encourage more investments in areas such as durable goods, education, houses, personal transportation and business. Presently, consumer spending accounts for 70.0% of the Philippines GDP. Growth in consumer loans will be further fueled by banks' aggressive attitude towards developing and increasing their loan portfolios, accommodating consumers in different socio-economic classes.

Among the ASEAN 5 economies, Philippine banks have the lowest exposure to consumer credit, thus indicating that the consumer market still presents very good opportunities for the country's banking industry. As a percentage of total loan portfolio (TLP), the 16.6% consumer credit exposure of Philippine banks as of end-2015 was lower compared with Malaysia (56.8% CL exposure), Thailand (28.8%), Indonesia (28.0%) and Singapore (26.6%).

ASSET QUALITY

Growth in loan portfolio counterbalanced the increase in NPLs and repossessed assets, resulting in lower NPA ratio, as of end-2015. The increase in NPA, combined with lower loss reserves, resulted in a lower coverage ratio as of December 31, 2015. Still, reserve coverage was considered more than adequate, given that PSBank has managed to keep its NPA ratios at low single-digit levels in past years.

Loans posted a hike of 17.9% to P116.0 billion in 2015, and which was much faster compared to the 15.0% growth in 2014. PSBank continued to benefit from the consumer-led growth of the domestic economy, particularly in auto loans where overall industry sales grew by 22.9% to 288,609 units. Auto loans of PSBank posted a marked increase of 30.4% to P59.3 billion. The bank's mortgage loan portfolio, on the other hand, similarly went up by 18.0% to P40.1 billion.

PhilRatings believes that PSBank's loan portfolio growth will be sustained, at least in the short-term, as domestic economic expansion continues to be supported by consumer demand in real estate, renting, and business activities. PSBank is particularly bullish on its auto loans business, given that almost 80.0% of sales in the auto loans sector are financed. As of March 31, 2016, about 66.0% of total assets were represented by loans and receivables. PSBank's top ten largest loan exposures represented a minimal portion of the bank's loan portfolio, and were all current as of report writing date. Non-lending assets were generally liquid, consisting of government and private securities.

The breakdown of PSBank's loan portfolio was in line with its market identity as a consumer-focused bank. Consumption loans and real estate loans accounted for 51.8% and 35.1%, respectively of customer loans, as of end-2015. Commercial loans had a share of 10.0%, while personal loans took the balance of 3.1%. Personal loans were comprised of deposit collateral loans, employee salary and consumer loan products such as money card, multi-purpose loan and flexi-loan.

Based on industry, Activities of households as employers and undifferentiated goods-and-services producing activities of households for own use accounted for bulk of customer loans at 56.9%, as of December 31, 2015. Real estate activities had the second largest share, at 31.4%. Other economic activities had shares of less than 5.0%.

About 77.8% of PSBank's customer loans were secured as of end-2015, and which was a positive to the bank's credit standing. Loans collateralized by chattel and real estate represented 66.7% and 32.5%, respectively of the bank's total secured loans.

PROFITABILITY

Audited 2015

PSBank ended 2015 with a net income of P2.4 billion, representing an almost flat growth of 1.4% from its bottom line in 2014. The almost flat earnings growth, coupled with the 16.3% increase in total assets, resulted in marginally lower ROAA in 2015. Recorded ROAA in 2015 was 1.5%, down from 1.7% in 2014.

Net interest income went up by 10.0% to P8.5 billion, mainly attributable to higher interest income from Loans and Receivables. Revenue growth, however, was minimal at 2.2% due to an 18.9% decline in non-interest Income. PSBank registered a trading loss of P63.6 million in 2015, a reversal of its P210.0 trading gains in 2014. Also, results in 2014 also included a substantial one-time gain of P558.7 million from the sale of PSBank's interest in Toyota Financial Services Corporation (TFSC) to GTCap. The sale was in line with PSBank's capital planning initiatives under the new Basel III regime. Excluding gains from the TFSC sale, non-interest Income would show a minimal hike of less than 1.0% in 2015. Non-interest income accounted for 21.5% of revenues in 2015, a noticeable decline from its 27.0% share in 2014.

Expense to average assets ratio improved to 4.4%, from 4.8% in 2014. Operating expenses (opex, excluding provision for losses) increase was a minimal 4.8% in 2015, and indicating that management of PSBank's opex continued to be largely controlled even as the bank undertook expansion activities.

Interim March 2016

PSBank ended 1Q2016 with a net income of P434.8 million, up by 12.3% from a year-ago. On a pre-tax basis, net income recorded a marginal increase of 5.2% to P437.1 million.

Revenues went up by 17.7% to P3.0 billion, as both net interest and non-interest incomes posted increases for the quarter. Net interest income grew by 14.3% to P2.3 billion, largely driven by the 10.9% increase in Interest income on Loans and Receivables. Non-interest income posted a much faster growth of 28.5% to P790.6 million, as the bank recorded trading gains of P269.9 million from P3.3 million trading loss in the same period of 2014. Higher revenues, however, was counterbalanced by a 14.1% increase in opex (excluding provision for losses) to P2.0 billion. Compensation and fringe benefits went up by 24.8% to P807.4 million, due to CBA-related benefits given to employees.

Results in the 1Q2016 translated to an ROAA of 1.0%, which was slightly lower compared with 1.1% in 1Q2015.

Projections 2016-2017

Projections for 2016 show a moderate growth in net income. Forecast net interest income growth is within historical levels, but non-interest income is projected to post a significant increase due to gains from trading and the foreclosure of investment properties. Offsetting the impact of higher revenues to earnings is the hike in total expenses in 2016, mainly attributable to increases in personnel-related expenses and provision for credit losses. The projected increase in provision for credit losses is in line with the growth of the bank's loan portfolio.

Net income is expected to post a much bigger increase in 2017, as total non-interest expenses growth substantially slows down. All non-interest expense items, except for provision for credit losses, are anticipated to post single-digit growths in 2017. Projected revenues will post a modest growth attributable to lower trading gains. Net interest income will continue to account for the bulk of revenues. Forecast ROAA in 2016 and 2017 will be within historical levels. Cost management will remain satisfactory.

ASSET-LIABILITYMANAGEMENT

PSBank's funding base predominantly consisted of customer deposits, and demonstrated a low reliance on wholesale sources. Deposits to liabilities ratio stood at 87.9% as of end-March 2016, slightly lower from end-2015 ratio of 89.4%. Loans to deposit ratio, however, was almost unchanged at 86.4%, indicating that deposit growth largely kept up with loan portfolio expansion. Bills payable, comprised of interbank borrowings and securities sold under repurchase agreements, went up by 59.8% to P7.2 billion as of March 31, 2016.

CASA accounted for 27.4% of total deposits as of end-March 2016, comparatively less than the share of time deposits. CASA, however, posted a much faster increase of 4.9% against the 0.6% hike in time deposits. These developments are considered as credit positives, since CASA is viewed as a more stable and less expensive funding source than time deposits.

The increasing share of CASA to total deposits is expected to hold for 2016 and 2017, supported in large part by the bank's continued branch expansion (and consequently, increasing recognition of the PSBank brand), as well as its continued incentive programs. As of end-2015, PSBank had the largest branch network in the TB sector.

CAPITAL

As of end-2015, PSBank's CAR of 18.0% was highest among PRS-rated banks: UnionBank of the Philippines (UnionBank, CAR of 16.2%), East West Banking Corporation (EastWest Bank, 15.6%), and AUB (13.8%). UnionBank and EastWest Bank have issuer ratings of PRS Aaa (corp.) and PRS Aa plus (corp.), respectively from PhilRatings. The issuer rating of AUB is PRS Aa (corp.).

PSBank ended the 1Q2016 with equity of P19.7 billion, which was also higher compared with the equity of some domestic KBs. Equity to assets ratio of PSBank stood at 11.2% as of March 31, 2016, almost unchanged from end-2015 ratio of 11.3%. CAR of 15.0%, albeit lower from end-2015 ratio of 18.0%, was still above the minimum regulatory requirement of 10.0%. Forecast CAR for 2016 and 2017will remain above 10.0%. The projected increase in equity will result from the plowback of earnings into operations.