

Media Release:

# Next Commercial Bank Co. Ltd. Assigned 'twA+/twA-1' Ratings, Outlook Stable

April 29, 2022

## Overview

- We forecast Next Commercial Bank Co. Ltd. (Next Bank) will maintain very strong capitalization and a satisfactory liquid assets position over the next two years as a new start up virtual bank with high paid-up capital relative to its small operating scale during its early years.
- We view Next Bank as a strategically important entity of the **Chunghwa Telecom Co. Ltd.** group, which is the largest shareholder in Next Bank, given the bank's importance to the group's long-term strategy to broaden the group's technology business scope.
- We are assigning our 'twA+' long-term and 'twA-1' short-term issuer credit ratings to Next Bank.
- The stable rating outlook reflects our view that Next Bank will remain a strategic important unit to Chunghwa Telecom group, and our assessment that the bank will maintain very strong capitalization over the next two years.

## Rating Action

Taiwan Ratings Corp. today assigned its 'twA+' long-term and 'twA-1' short-term issuer credit ratings on Next Bank. The outlook on the long-term rating is stable

## Rationale

The ratings on Next Bank reflect the bank's very strong capitalization relative to its risk profile, adequate liquidity backed by sizeable highly liquid assets, as well as potential technical support from its two major shareholders--Taiwan-based Chunghwa Telecom and **Mega International Bank Co. Ltd.** The ratings also reflect our view of a very high likelihood that Chunghwa Telecom would provide support for Next Bank, given our assessment of the bank's strategic importance to the group. These strengths are somewhat tempered by Next Bank's limited market presence and developing franchise in Taiwan's highly competitive banking sector, as well as the bank's untested risk control capacity as one of the first Internet-only banks in Taiwan.

In our view, Next Bank's business position during its initial operating stage is significantly weaker than the domestic banking average and reflects Next Bank's limited operating scale, developing franchise, and evolving customer base over the next two years. Based on the

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bank's business plan, its asset size is likely to remain small until the end of 2024. It will take time for Next Bank to build a more stable, seasoned business profile under the highly competitive banking sector in Taiwan. Moreover, Next Bank's business diversity will be somewhat weaker than the industry average, given the bank's initial focus on selective businesses under current regulations.

However, the potential resource support from major shareholders including Chunghwa Telecom and Taiwan-based supermarket chain PX Mart could somewhat support a steady business flow during the bank's early operating years. That's because both shareholders have a strong client base in Taiwan from which to seek new users for the bank.

We see Next Bank gradually consuming its paid-up capital of new Taiwan dollar (NT\$) 10 billion during its growth phase but still maintain very strong capitalization over the next two years. We estimate the bank's risk-adjusted capital (RAC) ratio before diversification will be 51.2% in December 2022. We believe the ratio will remain above 15% until 2024, despite very high growth and operating losses during the period. The bank's profitability will be below the industry average during its early years of operation, constrained by its small business scale and high initial operating expenses. We also believe it will take several years for Next Bank to achieve better economies of scale and turn profitable.

It will likely take considerable time for Next Bank to season its portfolio, given the quick expansion of its asset book and dynamic product offering strategy in the early operating period. In this regard, Next Bank's risk position has a limited track record compared with more established banks in Taiwan that possess long operating records and seasoned portfolios. We also forecast that during its expansionary stage Next Bank's growth appetite will be more aggressive than the bank average in Taiwan. Nonetheless, most of the bank's new business will be relatively simple retail banking and fee-generated business; therefore, the potential risks should be manageable. The key risk for Internet-only banks such as Next Bank, relates to information security and cyber risk, which are yet to be tested in an increasingly dynamic virtual environment.

We view Next Bank's funding capacity to be below the average of the more established banks in Taiwan, and its liquidity profile to be adequate. As a new player, Next Bank needs to build up its brand recognition and franchise in the domestic market, which is very competitive. The bank does not have a branch network; therefore, it can only rely on the Internet to acquire retail depositors. Next Bank may need two to three years along with good product differentiation to establish a more meaningful, retentive deposit base.

We assess the bank's liquidity to be satisfactory, considering its holdings of sizeable liquid assets. The projected loan to deposit ratio is likely to be lower than the domestic peer average by 2024, in our view. Most of the bank's funds are likely to be allocated to highly liquid fixed-income securities with good asset quality.

ESG credit factors are neutral to our ratings on Next Bank. The bank has set up corporate social responsibility principles as a guideline to fulfill related goals. The ESG framework and implementation details will be gradually rolled out during the bank's early phase of operations. We believe Next Bank could leverage the extensive experience of its major shareholders in these fields to support its development plan.

We view Next Bank as a strategically important entity to Chunghwa Telecom. This reflects Next Bank's importance to Chunghwa Telecom's long-term strategy to provide value-added

digital services linked with the burgeoning financial technology (fintech) environment, which could help enhance customer retention and broaden the group's technology business scope. We do not expect Chunghwa Telecom to divest of the bank, given its important strategic fit.

Next Bank is one of the three Internet-only banks approved by Taiwan's regulator in mid-2019. The major shareholders are Chunghwa Telecom (41.9%), Mega International Bank (25.1%), Shin Kong Life Insurance Co. Ltd. (10%), PX Mart (9.9%), and KGI Bank (7%). The bank has initial paid-up capital of NT\$ 10 billion.

## Outlook

The stable rating outlook reflects our view that Next Bank will maintain its strategic importance to Chunghwa Telecom over the next two years. We also forecast the bank will maintain very strong capitalization over the same period, despite potentially strong business growth and operating losses during its expansionary stage. Moreover, we believe the bank will maintain adequate liquidity and leverage the resources of its major shareholders to support growth in its business operations and risk controls over the same period.

### Downward scenario

We may lower the long-term rating if:

- The bank's RAC ratio drops below 15% along with business expansion or unexpected operating losses for the next two years, if combined with a still-marginal market presence,
- Next Bank's asset quality weakens to become significantly worse than the industry average or the bank encounters cyber risk that incurs significant financial losses or franchise damage, or
- Chunghwa Telecom demonstrates its intention to reduce its shareholding in the bank or lessens its commitment to support the bank's operations.

### Upward scenario

We may raise the rating if:

- Next Bank can enhance its market presence, demonstrates more stable business stability, and satisfactory risk control capacity over the next two years. At the same time, the bank would need to maintain its capitalization at a very strong level, or
- Next Bank becomes a highly strategic entity of the Chunghwa Telecom group, although we view the possibility of this to be low for the next two years. That's because the bank needs more time to demonstrate business integration with its shareholders or a meaningful contribution to the Chunghwa Telecom group during the early operating stage.

## Related Criteria & Research

### Related Criteria

- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings - October 10, 2021
- General Criteria: Principles Of Credit Ratings - February 16, 2011
- General Criteria: Methodology For National And Regional Scale Credit Ratings - June 25, 2018
- General Criteria: Group Rating Methodology - July 01, 2019
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings - April 07, 2017

- Criteria | Financial Institutions | Banks: Banking Industry Country Risk Assessment Methodology And Assumptions - December 09, 2021
- Criteria | Financial Institutions | General: Risk-Adjusted Capital Framework Methodology - July 20, 2017
- Criteria | Financial Institutions | General: Financial Institutions Rating Methodology - December 09, 2021

## Related Research

- Taiwan Ratings' Ratings Definitions – August 10, 2020

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## Ratings List

### New Ratings

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#### Next Commercial Bank Co. Ltd.

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Issuer Credit Rating	twA+/Stable/twA-1
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Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at [www.taiwanratings.com](http://www.taiwanratings.com) for further information. Complete ratings information is available to subscribers of Rating Research Service at [rrs.taiwanratings.com.tw](http://rrs.taiwanratings.com.tw). All ratings affected by this rating action can be found on Taiwan Ratings' public website at [www.taiwanratings.com](http://www.taiwanratings.com).

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