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ธนาคารกรุงไทย
KRUNGTHAI BANK

Management Discussion and Analysis

This report discusses principal changes in the audited consolidated financial statements for the three-month period ended June 30, 2016.

Thai economy expanded at gradual pace. Public spending showed a steady growth and tourism sector continued to expand. Moreover, domestic demand expanded resulting from higher spending from farm households after alleviating from drought conditions. However, the value of merchandise exports excluding gold remained contracted in line with the key trading partner countries' economy. As a result, overall manufacturing production and investment lingered at low level

The Bank and Its Subsidiaries' Performance

Performance for the first half of 2016

For the first half of 2016, KTB's consolidated operating profit was Bt 36,967 m, increased by Bt 5,588 m (17.81%) from the same period of last year, attributed to the increase of net interest income by Bt 3,284m (8.16%) from maturity high-cost term deposit and appropriately managing of funding cost. Moreover, net fee and service income increased by Bt 1,603 m (17.94%) from ATM related business and electronic banking service fees.

NPLs continued to increase from the end of the year 2015 from corporate and SMEs clients combined with the retail sectors. Consequently, the first half of 2016, KTB's consolidated impairment loss on loans and debt securities amounted to Bt 16,364 m showing an increase of Bt 5,124 m (45.59%) from the same period of last year. The coverage ratio was 104.73% in accordance with the prudent banking practice to maintain coverage ratio at not less than 100%. KTB's consolidated net profit was Bt 16,823 m, decreased by Bt 71 m (0.42%) and net profit, attributable to equity holders of the Bank, was Bt 16,218 m, showing a decrease of Bt 160 m (0.98%) from the same period of last year.

Performance for the three-month period ended June 30, 2016

Operating Profit and Net Profit

KTB's consolidated operating profit was Bt 18,708 m, increased by Bt 1,250 m or 7.16% compared to 2Q2015. After deducting impairment loss on loans and debt securities and income tax expense, net profit was Bt 8,972 m, showing an increase of Bt 288 m or 3.32% compared to 2Q2015. Net profit, attributable to equity holders of the Bank, was Bt 8,679 m, showing an increase of Bt 230 m or 2.72% from 2Q2015.

Unit : Million Baht

	2Q2016	1Q2016	Change (%)	2Q2015	Change (%)
Operating profit*	18,708	18,259	2.46	17,458	7.16
Operating profit before tax	10,967	9,636	13.81	9,943	10.30
Income tax expense	1,995	1,775	12.39	1,259	58.46
Net profit	8,972	7,861	14.13	8,684	3.32
Net profit (attributable to equity holders of the Bank)	8,679	7,540	15.11	8,449	2.72

*Operating profit before Impairment loss of loans and debt securities

Net Interest Income

KTB's consolidated net interest income equaled Bt 22,177 m, showing an increase of Bt 1,282 m (6.14%) from 2Q2015 due to the maturity of high-cost fixed deposit as well as appropriate funding cost management. Consequently, Net Interest Margin (NIM) rose to 3.28% from 3.11% in 2Q2015.

Unit : Million Baht

	2Q2016	1Q2016	Change (%)	2Q2015	Change (%)
Interest income	32,920	32,666	0.78	33,937	(3.00)
- Interbank and money market items	2,839	2,791	1.72	3,049	(6.89)
- Investments and trading transactions	34	26	30.77	106	(67.92)
- Investment in debt securities	1,739	679	156.11	1,501	15.86
- Loans	27,534	28,336	(2.83)	28,343	(2.85)
- Hire purchase and financial lease	765	823	(7.05)	932	(17.92)
- Others	9	11	(18.18)	6	50.00
Less Interest expense	10,743	11,325	(5.14)	13,042	(17.63)
- Deposits	6,317	6,852	(7.81)	8,612	(26.65)
- Interbank and money market items	670	706	(5.10)	723	(7.33)
- Contributions to BOT and DPA	2,445	2,460	(0.61)	2,522	(3.05)
- Debts issued	1,297	1,290	0.54	1,176	10.29
Debenture	1,214	1,212	0.17	1,072	13.25
B/E	83	78	6.41	104	(20.19)
- Borrowings	7	7	0.00	7	0.00
- Others	7	10	(30.00)	2	250.00
Net interest income*	22,177	21,341	3.92	20,895	6.14
Net interest margin [based on earning assets] (%)	3.28	3.17		3.11	

*The Bank has reclassified fee from loan from one of KTB's subsidiaries, thus some fee from loan in interest income were grouped as fee income since 3Q2015 onwards. Nonetheless, if restates Statements of income and other comprehensive income of 2Q2015, the net interest income and net fee income will be Bt 20,307 m and Bt 5,193 m respectively. Thus, the net interest income and net fee income growth of 2Q2016, compare to 2Q2015, will be Bt 1,870 m (9.21%) and Bt 138 m (2.66%) respectively

	30 Jun 2016	31 Mar 2016	31 Dec 2015	30 Sep 2015	30 Jun 2015
Policy Interest Rate (%)	1.50%	1.50%	1.50%	1.50%	1.50%
Deposit Rate (%)					
- Saving Rate	0.50%	0.50%	0.50%	0.50%	0.50%
- 3 Months Fixed Rate	0.90%	0.90%	0.90%	0.90%	0.90%
- 6 Months Fixed Rate	1.35%	1.35%	1.35%	1.35%	1.35%
- 12 Months Fixed Rate	1.40%	1.50%	1.50%	1.50%	1.50%
Loan Rate (%)					
- MLR	6.275%	6.525%	6.525%	6.525%	6.525%
- MOR	7.120%	7.375%	7.375%	7.375%	7.375%
- MRR	7.620%	7.875%	7.875%	7.875%	7.875%

Net Fee and Service Income

KTB's consolidated net fee and service income in 2Q2016 amounted to Bt 5,331 m, increased by Bt 726 m (15.77%) from 2Q2015 in response to the fee expansion from ATM related business as well as electronic banking service fees.

Unit : Million Baht

	2Q2016	1Q2016	Change (%)	2Q2015	Change (%)
Fee and service income	6,394	6,130	4.31	5,335	19.85
Less Fee and service expense	1,063	921	15.42	730	45.62
Net fee and service income*	5,331	5,209	2.34	4,605	15.77

*The Bank has reclassified fee from loan from one of KTB's subsidiaries, thus some fee from loan in interest income were grouped as fee income since 3Q2015 onwards. Nonetheless, if restates Statements of income and other comprehensive income of 2Q2015, the net interest income and net fee income will be Bt 20,307 m and Bt 5,193 m respectively. Thus, the net interest income and net fee income growth of 2Q2016, compare to 2Q2015, will be Bt 1,870 m (9.21%) and Bt 138 m (2.66%) respectively

Total Other Operating Income

KTB's consolidated total other operating income in 2Q2016 amounted to Bt 3,384 m, decreased by Bt 724 m (17.62%) from 2Q2015. The main reasons were the reduction of the share of profit from investments on equity method by Bt 388 m (41.68%) from diminishing in profit of insurance related bank's subsidiaries, and the decline in net gain on trading and foreign exchange transaction by Bt 226 m (11.80%) from the decrease in global market services income as a result of the money market trend.

Unit : Million Baht

	2Q2016	1Q2016	Change (%)	2Q2015	Change (%)
Gain (loss) on trading and foreign exchange transactions, net	1,689	1,827	(7.55)	1,915	(11.80)
Gain (loss) on investments, net	237	338	(29.88)	328	(27.74)
Share of profit (loss) from investments on equity method	543	559	(2.86)	931	(41.68)
Dividend income	157	116	35.34	78	101.28
Other income	758	1,333	(43.14)	856	(11.45)
Total other operating income	3,384	4,173	(18.91)	4,108	(17.62)

Other Operating Expenses

KTB's consolidated other operating expenses in 2Q2016 amounted to Bt 12,184 m, increased by Bt 34 m (0.28%) from 2Q2015 mainly from an increasing in personnel expense by Bt 252 m (3.88%), while taxes and duties, and premises and equipment expenses declined. Therefore, Cost-to-Income Ratio reduced to 39.44%, from 41.04% in 2Q2015, as a result of the expansion of operating income along with the flat operating expense.

Unit : Million Baht

	2Q2016	1Q2016	Change (%)	2Q2015	Change (%)
Personnel expenses	6,744	7,715	(12.59)	6,492	3.88
Directors' remuneration	67	15	346.67	73	(8.22)
Premises and equipment expenses	2,222	2,067	7.50	2,276	(2.37)
Taxes and duties	1,125	1,238	(9.13)	1,258	(10.57)
Others	2,026	1,429	41.78	2,051	(1.22)
Total other operating expenses	12,184	12,464	(2.25)	12,150	(0.28)
Cost-to-income ratio (%)	39.44	40.57		41.04	

Impairment Loss of Loans and Debt Securities

The consolidated impairment loss of loans and debt securities amounted to Bt 7,741 m, increased by Bt 226 m (3.01%), compared to 2Q2015. For the bank only basis, the Bank set aside Bt 6,000 m for impairment loss of loans and debt securities. In 2016, the Bank's monthly normalized provision increased from Bt 700 m to Bt 1,000 m in accordance with the consideration of outstanding loans and economic situation. Furthermore, the Bank's additional provision was provided in amount of Bt 3,000 m as a consequence of the incremental NPLs.

Therefore, KTB's consolidated coverage ratio dropped to 104.73% from 112.55% and for the banking basis, coverage ratio was 102.66%, decreased from 110.54% as at the end of the year 2015

Unit : Million Baht

	2Q2016	1Q2016	Change (%)	2Q2015	Change (%)
Impairment loss of loans and debt securities	7,741	8,623	(10.23)	7,515	3.01

The Bank and Its Subsidiaries' Financial Status

As at the period ended June 30, 2016

Loans to Customers

KTB's consolidated total loans to customers (less deferred revenue) stood at Bt 1,973,366 m which reduced by Bt 54,074 m (2.67%) from end of year 2015, as a consequence of the contraction of all major sectors excepting corporate sector. Moreover, net Interbank and money market items expanded by Bt 97,463 m (24.53%) resulting in total asset raised in amount of Bt 15,518 m (0.55%) from the end of 2015, to be Bt 2,830,848 m as of June 30, 2016

- Loan portfolio breakdown by borrowers

Unit : Million Baht

The Bank's Financial Statements	Jun 30, 2016		Dec 31, 2015		Change
	Amount	(%)	Amount	(%)	(%)
Private Corporate	690,674	36.08	685,253	34.79	0.79
Government and State Enterprise	103,690	5.42	129,865	6.59	(20.16)
SMEs*	400,355	20.92	429,125	21.79	(6.70)
Retail	718,840	37.56	725,122	36.81	(0.87)
Others	476	0.02	462	0.02	3.03
Total loans	1,914,035	100.00	1,969,827	100.00	(2.83)
Less Deferred revenue	196		166		
Total	1,913,839		1,969,661		

*SMEs were private companies that have employee no. less than/equal to 200 people and fixed asset (excluding land) less than/equal to Bt 200 m.

- Loan portfolio breakdown by industry

Unit : Million Baht

	Jun 30, 2016		Dec 31, 2015		Change
	Amount	(%)	Amount	(%)	(%)
Agriculture and mining	41,608	2.11	40,082	1.98	3.81
Manufacturing and commerce	569,207	28.84	577,718	28.49	(1.47)
Real estate and construction	130,383	6.61	146,830	7.24	(11.20)
Public utilities and services	317,250	16.08	394,721	19.47	(19.63)
Housing loans	372,080	18.85	381,950	18.84	(2.58)
Others	542,838	27.51	486,139	23.98	11.66
Total loans	1,973,366	100.00	2,027,440	100.00	(2.67)

Investments

KTB's consolidated net investments as of June 30, 2016 totaled Bt 243,047 m, declined by Bt 18,685 m (7.14%) from the end of last year.

Unit : Million Baht

	Jun 30, 2016		Dec 31, 2015		Change
	Amount	(%)	Amount	(%)	(%)
Investments, net	223,118	91.80	247,082	94.40	(9.70)
Investments in subsidiaries and associates, net	19,929	8.20	14,650	5.60	36.03
Total investments, net	243,047	100.00	261,732	100.00	(7.14)

Total Assets

KTB's consolidated total assets as at June 30, 2016 was Bt 2,830,848 m, rose by Bt 15,518 m (0.55%) from December 31, 2015, owing to the expansion of net interbank and money market items by Bt 97,463 m (24.53%) from its liquidity position, offsetting the reduction of net loans to customers.

Liabilities

KTB's consolidated deposits totaled Bt 2,081,903 m, decreased by Bt 53,595 m (2.51%) from December 31, 2015 due to the maturity of term deposit, consistent with the contraction of loans. Its consolidated loans to customers (less deferred revenue) -to-deposits ratio was 94.79%, stable at 94.94% compared with the end of the year 2015. On the contrary, the Bank's consolidated net interbank and money market item were Bt 228,472 m, increased by Bt 34,229 m (17.62%). Thus, KTB's consolidated liabilities totaled Bt 2,564,957 m, steady to December 31, 2015.

	Unit : Million Baht				
	Jun 30, 2016		Dec 31, 2015		Change
	Amount	(%)	Amount	(%)	(%)
Demand deposits	91,829	4.41	126,974	5.95	(27.68)
Savings deposits	1,195,697	57.43	1,147,811	53.75	4.17
Time deposits	794,377	38.16	860,713	40.30	(7.71)
Total Deposits	2,081,903	100.00	2,135,498	100.00	(2.51)
B/E	7,691		6,735		

Equity

The total equity (Equity holders of the Bank) as at June 30, 2016 amounted to Bt 261,286 m, showing an increase of Bt 15,403 m (6.26%) from December 31, 2015.

Book value per share (Equity holders of the Bank) was Bt 18.69, raised from Bt 17.59 as at December 31, 2015.

Sources and Uses of Funds

As of June 30, 2016, 73.55% of the Bank's source of funds was deposits; the rests were interbank borrowings, debt issued and borrowings, and equity. The Bank's use of funds comprised of 69.71% loans to customers (less deferred revenue), 17.48% net interbank and money market items, and 8.59% net investments and net investments in subsidiaries and associates.

	Unit : Million Baht				
	Jun 30, 2016		Dec 31, 2015		Change
	Amount	(%)	Amount	(%)	(%)
Deposits	2,081,903	73.55	2,135,498	75.85	(2.51)
Interbank and money market items, net	228,472	8.07	194,243	6.90	17.62
Debt issued and borrowings	120,048	4.24	116,240	4.13	3.28
Others	134,534	4.75	119,051	4.23	13.01
Total equity					
- Equity holders of the Bank	261,286	9.23	245,883	8.73	6.26
- Non-controlling interest	4,605	0.16	4,415	0.16	4.30
Total	2,830,848	100.00	2,815,330	100.00	0.55

Unit : Million Baht

Loans and deposits classified by remaining maturity The Bank's Financial Statements	Jun 30, 2016		Dec 31, 2015		Change (%)
	Amount	(%)	Amount	(%)	
Loans					
- ≤ 1 year	676,366	35.34	652,664	33.14	3.63
- > 1 year	1,237,669	64.67	1,317,163	66.87	(6.04)
Less Unearned Discounts	196	0.01	166	0.01	
Total loans *	1,913,839	100.00	1,969,661	100.00	(2.83)
Deposits					
- ≤ 1 year	1,922,633	92.28	1,946,713	91.08	(1.24)
- > 1 year	160,899	7.72	190,733	8.92	(15.64)
Total deposits	2,083,532	100.00	2,137,446	100.00	(2.52)

* Excluding accrued interest receivable and interbank loans and money market item.

Statutory Capital Fund

As at June 30, 2016, Common Equity Tier 1 capital was Bt 225,381 m (11.68% of its risk-weighted assets (RWA)) and Tier 1 capital was Bt 231,763 m (12.02% of its risk-weighted assets (RWA)). Bank's capital totaled Bt 305,617 m (15.84% of its risk-weighted assets (RWA)), increased from 15.22% at December 31, 2015. The calculation was in line with BOT's regulations regarding Basel III compliance.

Unit : Million Baht

The Bank's Financial Statements	June 30, 2016			December 31, 2015		
	Amount	(%)	The minimum rate required by the BOT (%)*	Amount	(%)	The minimum rate required by the BOT (%)
Common Equity Tier 1 capital	225,381	11.68	5.125	217,646	11.06	4.50
Tier 1 capital	231,763	12.02	6.625	225,092	11.43	6.00
Tier 2 capital	73,854			74,529		
Total capital fund	305,617	15.84	9.125	299,621	15.22	8.50
Risk-weighted assets	1,928,834			1,968,708		

* According to BOT's regulation, the minimum capital ratios of Commercial Banks in Thailand will be increased to absorb Capital conversation buffer at 0.625 percent starting from January 1, 2016 until reaches 2.5 percent by January 1, 2019.

Asset Quality - Non-Performing Loans

KTB's consolidated NPLs as at June 30, 2016 stood at Bt 94,217 m, increased by Bt 17,846 m (23.37%) from December 31, 2015. The NPLs ratio (gross) and NPL ratio (net) were 3.89% and 1.94% respectively. The increase of NPLs was partly from corporate clients combined with the increase of NPLs from SME and Retail sectors in line with the slow economy recovery. However, the Bank focused more on the collection process along with the effective debt restructuring to cope with its deteriorated asset quality.

On the bank-only basis, the NPLs was Bt 89,467 m, showing an increase of Bt 17,619 m, or 24.52% from December 31, 2015.

Unit : Million Baht

NPLs classification and provision coverage	Jun 30, 2016		Dec 31, 2015		Change
	Amount	(%)	Amount	(%)	
1. Loans					
Pass	1,838,726	93.17	1,899,234	93.68	(3.19)
Special Mention	40,423	2.05	51,835	2.56	(22.02)
Sub-Standard	18,504	0.94	18,722	0.92	(1.16)
Doubtful	25,637	1.30	19,004	0.94	34.90
Doubtful of loss	50,076	2.54	38,645	1.90	29.58
Total Loans	1,978,366	100.00	2,027,440	100.00	(2.67)
2. NPLs gross ⁽¹⁾	94,217	3.89	76,371	3.20	23.37
NPLs net ⁽¹⁾	45,944	1.94	40,612	1.73	
3. Actual provisioning for loan loss ⁽²⁾	98,672		85,956		14.79
Coverage Ratio		104.73		112.55	

(1) NPLs Ratio (gross) and NPLs Ratio (net) from BOT definition

(2) Allowance for doubtful accounts and revaluation allowance for debt restructuring

Unit : Million Baht

NPLs (gross) breakdown by industry	Jun 30, 2016		Dec 31, 2015	
	Amount	(%)	Amount	(%)
Agriculture and mining	1,202	1.28%	1,220	1.60
Manufacturing and commerce	44,937	47.69%	33,835	44.30
Real estate and construction	11,975	12.71%	11,573	15.15
Public utilities and services	10,818	11.48%	8,056	10.55
Housing loans	14,856	15.77%	12,629	16.54
Others	10,429	11.07%	9,058	11.86
Total NPLs (gross)	94,217	100.00%	76,371	100.00

Credit Ratings

Bank's credit ratings rated by Standard and Poor's, Moody's Investors Service and Fitch Ratings were as follows:

<ul style="list-style-type: none"> ■ Standard & Poor's 	June 2016	December 2015
<ul style="list-style-type: none"> ▪ Long-term/ Short-term 	BBB / A-2	BBB / A-2
<ul style="list-style-type: none"> ▪ Outlook 	Stable	Stable
<ul style="list-style-type: none"> ▪ Stand-Alone Credit Profile (SACP) 	bb+	bb+
<ul style="list-style-type: none"> ▪ Hybrid Tier 1 (USD) 	B+	B+
<ul style="list-style-type: none"> ■ Moody's Investors Service 	June 2016	December 2015
<ul style="list-style-type: none"> ▪ Long-term/ Short-term 	Baa1 / P-2	Baa1 / P-2
<ul style="list-style-type: none"> ▪ Outlook 	Stable	Stable
<ul style="list-style-type: none"> ▪ Baseline Credit Assessment (BCA) 	ba1	ba1
<ul style="list-style-type: none"> ▪ Hybrid Tier 1 (USD) 	B1	B1
<ul style="list-style-type: none"> ■ Fitch Ratings 	June 2016	December 2015
Foreign Currency Credit Ratings		
<ul style="list-style-type: none"> ▪ Long-term/ Short-term 	BBB / F3	BBB / F3
<ul style="list-style-type: none"> ▪ Outlook 	Stable	Stable
<ul style="list-style-type: none"> ▪ Viability Rating 	bbb-	bbb-
<ul style="list-style-type: none"> ▪ Subordinated Debt (USD) 	BBB-	BBB-
<ul style="list-style-type: none"> ▪ Hybrid Tier 1 (USD) 	B	B
National Credit Ratings		
<ul style="list-style-type: none"> ▪ Long-term/ Short-term 	AA+(tha) / F1+ (tha)	AA+(tha) / F1+ (tha)
<ul style="list-style-type: none"> ▪ Outlook 	Stable	Stable
<ul style="list-style-type: none"> ▪ Subordinated Debt (Baht) 	AA(tha)	AA(tha)
<ul style="list-style-type: none"> ▪ Hybrid Tier 1 (Baht) 	BBB(tha)	BBB(tha)