

ASIA SERMKIJ LEASING PLC

No. 162/2020
12 October 2020

FINANCIAL INSTITUTIONS

Company Rating: BBB+
Outlook: Stable

Last Review Date: 15/10/19

Issue Rating History:

Date	Rating	Outlook/Alert
07/10/08	BBB+	Stable

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RATIONALE

TRIS Rating affirms the company rating on Asia Sermkij Leasing PLC (ASK) at “BBB+” with a “stable” outlook. The rating reflects ASK’s moderate and steady business growth, manageable asset quality, ability to maintain operating performance, as well as the business and financial support it receives from its major shareholders. The rating is constrained by the company’s moderate capital level, relatively high financial leverage, and the pressure on profitability due to intense competition and the weak economy.

KEY RATING CONSIDERATIONS

Steady growth in market position

The company has been able to improve its market position continuously, as shown by the steady growth in its loan portfolio over the last few years. ASK’s outstanding loans rose to THB41.3 billion at the end of December 2019, up 15% from THB35.9 billion for the same period of the previous year, through its marketing efforts and expanding market coverage with two new branches opened in 2019. At the end of June 2020, outstanding loans grew by 2% year-to-date to THB42.1 billion mainly driven by growth in used commercial truck loans and auto title loans. The company targeted borrowers in the logistics and agriculture-related industries that are less vulnerable during the Coronavirus Disease 2019 (COVID-19) outbreak.

We project ASK’s new loan portfolio to expand by 2.8% in 2020 and 3.7% annually between 2021-2022. We expect auto financing loans and auto title loans will continue to support growth, particularly in its core business of used trucks in the logistics segment whose demand remains robust despite the economic slowdown.

Overall asset quality should remain sound despite potential deterioration

We expect the company to maintain its prudent credit policies and efficient debt collection processes to help control potential credit losses particularly amid the COVID-19 economic fallout. Nonetheless, we expect the company to still be impacted by the potential deterioration of asset quality, with our estimate of credit cost at around 1.4%-2% per annum between 2020-2022.

At the end of June 2020, the company’s non-performing loan (NPL) coverage ratio based on TFRS9 slightly decreased to 3.1%, from 3.45% in 2019. Nonetheless, this NPL level is considered low compared with industry peers. The credit cost for 2019 and the first quarter 2020 (annualized) was at 1.2%.

At the end of June 2020, the company’s NPL coverage ratio based on TFRS9 standard increased to 74.9% from 67.9% in 2019.

Maintained earnings quality

We expect ASK’s earnings quality to be maintained over the next few years. The company’s earnings capability, measured by earnings before taxes to average risk-weighted assets (EBT/ARWA), was moderate with EBT/ARWA around 2.8% in 2018-2019. For the first six months of 2020, the company’s annualized EBT/ARWA ratio was 2.5%, with a net profit of THB431 million. In 2019, net income grew by 7% to THB870 million from 2018. The increase in net income was driven by higher net interest income, despite increased operating expenses and provision expenses.

We expect EBT/ARWA to stay around 2%-2.2% between 2020-2022. The earnings forecast is supported by our expectation that the company will maintain its interest spread while keeping its credit losses and operating expenses under control. This is despite intense competition in the commercial vehicle segment potentially resulting in decreasing yields. We expect the expansion into used commercial trucks and auto title loans, which could boost loan yields, and the decrease in funding cost will support the spread to stay around 4.5%-5% between 2020-2022. However, we expect credit costs between 2020-2022 to be slightly higher than the past due to the economic slowdown.

Capital base to be strengthened

ASK's risk-adjusted capital ratio (RAC) currently remains low, at 10.84% as of June 2020, which could limit its ability to expand its loans. Nonetheless, we expect its capital position to strengthen followed by a capital injection of THB2.5 billion in 2021. Taking this injection into account, we estimate its five-year average RAC for 2018-2022 to be at a moderate level of 15.4%. The stronger capital base should help support business expansion in the medium term.

In terms of financial leverage, its current debt to equity (D/E) ratio stood at 7.9 times at the end of June 2020, complying with its D/E covenant of 10 times.

Liquidity remains adequate despite high short-term debt obligations

We view the company as having a moderate liquidity profile. The company relies on short-term borrowings as its main source of funds to keep its funding costs low. This exposes the company to asset-liability mismatch and refinancing risk. At the end of June 2020, the company's short-term borrowings including current portion of long-term debts accounted for approximately 64% of total borrowings. Its liquidity coverage ratio (LCM) was weak at 0.01 times on a 2-year average. However, we expect ASK's back-up credit facilities from one of its shareholders, Bangkok Bank PLC (BBL), and other financial institutions will be sufficient to cover the outstanding short-term funding instruments it has issued in the capital market.

Adequate funding

The company's access to both debt and equity capital markets as well as credit facilities from financial institutions provides a variety of available funding sources that underpins its adequate funding profile. At the end of June 2020, the company had credit facilities from various financial institutions totaling THB37.7 billion, 18% of which were undrawn. It also receives soft loans of THB3.9 billion from the Government Savings Bank (GSB) to help support cash flow during the debt relief program.

BASE-CASE ASSUMPTIONS

TRIS Rating's base-case assumptions for ASK's performance in 2020-2022 are as follows:

- New loans to grow around 2.8% in 2020 and to expand by 3.7% annually thereafter.
- Loan spread to be maintained at 4.5%-5%.
- Credit cost to be around 1.4%-2%.

RATING OUTLOOK

The "stable" outlook is based on TRIS Rating's expectation that ASK will be able to maintain its market positions in commercial vehicle loans. The outlook takes into account a potentially stronger capital base and on-going support from its major shareholders. The outlook also factors in efficient risk management and operating systems to ensure that loan quality is preserved at the current level or improves further.

RATING SENSITIVITIES

The rating and/or outlook upside hinges on ASK's ability to strengthen its market position significantly, with steady loan quality, satisfactory financial performance, and a solid capital base with RAC more than 25%.

The rating and/or outlook could be revised downward should ASK's market position weakens materially, or if the company funds its growth by relying heavily on debt with RAC dropping below 9%. A significant deterioration in the NPL ratio or an interest spread below our expectation could adversely impact profitability and pressure the rating.

COMPANY OVERVIEW

ASK was established by the Bangkok Bank Group (BBL Group) in 1984, as an auto hire- purchase lender. ASK subsequently became a wholly-owned subsidiary of Bangkok Grand Pacific Lease PLC (BGPL). BGPL, which concentrates on leasing loans for machinery and equipment (M&E) and factoring loans to corporate clients, was established in 1989 by the BBL Group and Chailase Finance from Taiwan. However, ASK and its parent company, BGPL, both provided hire purchase loans. To

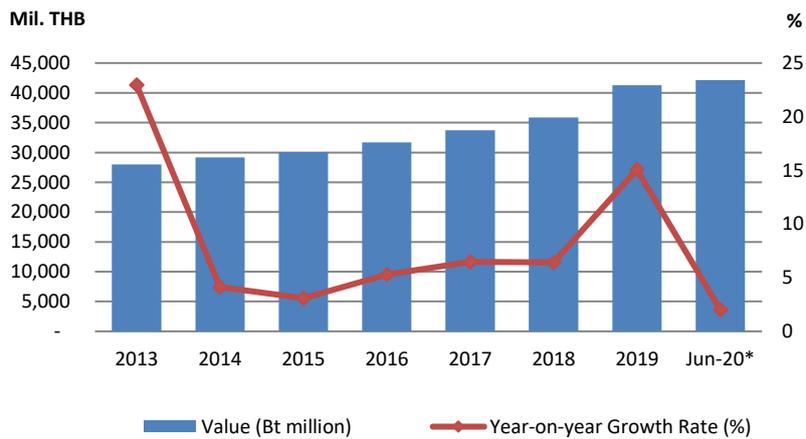
eliminate this conflict of interest, ASK's shareholding was restructured. BGPL became a wholly-owned subsidiary of ASK while BGPL's shareholders became ASK's shareholders. In 2005, ASK was listed on the Stock Exchange of Thailand (SET).

The Chailease Group from Taiwan holds a 49.9% stake in ASK. ASK is consolidated with Chailease Finance, based on the criteria of the power of control. Presently, the Chailease Group designates six directors to ASK's board and supports ASK's liquidity needs. The BBL Group, holding 10% stake in ASK, now supports ASK as a creditor rather than as an owner.

At the end of June 2020, approximately 80% of ASK's consolidated loan portfolio comprised retail auto financing loans. This proportion has held steady since 2010. ASK's wholly-owned subsidiary, BGPL, held machinery and equipment lease loans (14%) and other loans (6%).

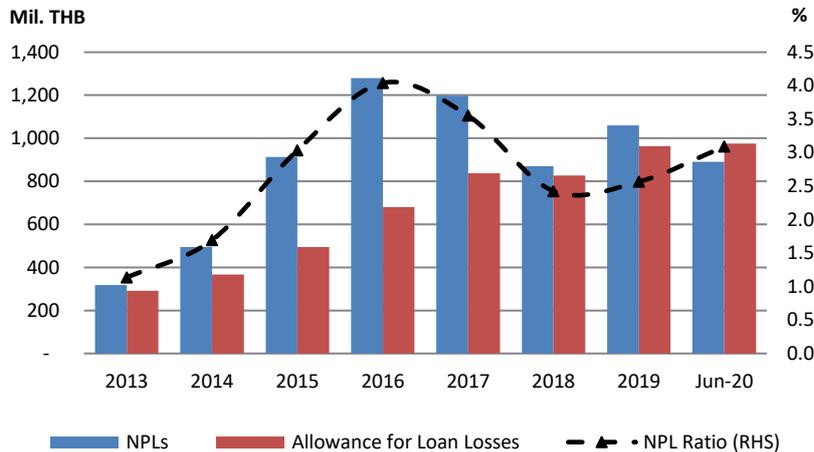
KEY OPERATING PERFORMANCE

Chart 1: Outstanding Loans



Source: ASK
* Year-to-date growth for Jun-20

Chart 2: Asset Quality



Source: ASK

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS*

Unit: Mil. THB

	Jan-Jun 2020	----- Year Ended 31 December -----			
		2019	2018	2017	2016
Total assets	46,447	41,815	36,252	33,999	31,707
Total loans	42,131	41,300	35,892	33,724	31,671
Allowance for doubtful accounts	975	964	827	837	681
Short-term borrowings	25,867	24,128	18,200	17,178	16,576
Long-term borrowings	14,288	11,126	12,024	11,139	9,773
Shareholders' equity	5,236	5,424	5,121	4,831	4,578
Net interest income	1,100	2,054	1,894	1,792	1,660
Bad debts and doubtful accounts	249	467	459	464	380
Non-interest income	185	433	425	369	326
Operating expenses	491	945	859	777	738
Net income	431	870	811	745	707

* Consolidated financial statements

Unit: %

	Jan-Jun 2020	----- Year Ended 31 December -----			
		2019	2018	2017	2016
Profitability					
Net-interest income/average assets	4.98 **	5.26	5.47	5.46	5.36
Net-interest income/total income	63.24	61.39	62.27	61.09	58.94
Operating expenses/total income	28.22	28.23	27.86	26.50	26.20
Operating profit/average assets	2.47 **	2.76	2.85	2.80	2.80
Earnings before taxes/average risk-weighted assets	2.50	2.69	2.79	2.74	5.32
Return on average assets	1.95 **	2.23	2.31	2.27	2.28
Return on average equity	16.17 **	16.49	16.30	15.84	15.84
Asset Quality					
Non-performing loans/total loans	3.09	2.57 ***	2.43	3.55	4.04
Bad debts and doubtful accounts/average loans	1.19 **	1.21	1.32	1.42	1.23
Allowance for doubtful accounts/total loans	2.31	2.33	2.30	2.48	2.15
Capitalization					
Risk-adjusted capital ratio	10.84	12.59	13.84	13.95	14.04
Shareholders' equity/total loans	12.43	13.13	14.27	14.32	14.46
Debt to equity (times)	7.87	6.71	6.08	6.04	5.93
Liquidity					
Stable funding ratio	90.28	65.57	78.95	79.94	77.26
Liquidity coverage measure (times)	0.17	0.02	0.01	0.02	0.01
Short-term borrowings/total liabilities	62.77	66.30	58.46	58.89	61.10
Total loans/total assets	90.71	98.77	99.01	99.19	99.89

* Consolidated financial statements

** Annualized

*** Based on the previous financial standard

RELATED CRITERIA

- Nonbank Financial Institution Methodology, 17 February 2020

Asia Sermkij Leasing PLC (ASK)

Company Rating:	BBB+
Rating Outlook:	Stable

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