

ASIA SERMKIJ LEASING PLC

No. 172/2021
15 October 2021

FINANCIAL INSTITUTIONS

Company Rating: BBB+
Outlook: Stable

Last Review Date: 12/10/20

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” rating outlook. The rating reflects ASK’s steady business growth, strong capital position, 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 intense competition in auto lending, and the weak economy induced by successive outbreaks of the Coronavirus Disease 2019 (COVID-19), which could pose a challenge to ASK’s ability to maintain its profitability and asset quality.

KEY RATING CONSIDERATIONS

Continuously expanding market position

The company continues to enhance its market position, as shown in the constant growth in its loan portfolio. At the end of June 2021, outstanding loans increased by 12% year-to-date to THB49.8 billion. The growth was driven by an aggressive marketing strategy, expansion into high-yield lending, mainly auto title loans, and by focusing on industries that are potentially less vulnerable to the COVID-19 pandemic, such as the medical, information technology (IT) and packaging sectors. ASK has also entered the solar energy segment after receiving knowhow from its major shareholder, the Chailease Group in Taiwan.

We expect ASK’s loan portfolio to expand progressively, with assumptions of 18% growth in 2021 and 9% per annum in 2022-2023. We believe that auto financing loans will continue to provide the major growth impetus for ASK, especially in its core business, the truck segment. The company’s expertise in this niche market and its focus on logistics and government-related construction segments that are less vulnerable during COVID-19 outbreaks should help sustain strong loan growth. At the end of June 2021, ASK’s outstanding retail auto loans, which comprised primarily loans for heavy trucks, accounting for around 70% of its loan portfolio. Other growth drivers are auto title loans and loans for working capital, which generate yields of around 10%-12%, higher than auto loans that generate 7%-8% yields.

Solid capital base

We expect ASK’s capitalization to remain strong over the next 2-3 years. The risk-adjusted capital (RAC) ratio was 15.1% at the end of June 2021, compared with 12.1% at the end of 2020. The stronger capital was due to a THB3 billion capital injection in June 2021, which should help support asset growth over the next 2-3 years. We forecast an RAC ratio in the range of 15%-17% in 2021-2023. Despite our strong loan growth assumption and a 60% dividend pay-out ratio, we believe consistent profit accumulation should strengthen the company’s capital position.

The debt to equity (D/E) ratio decreased to 4.9 times at the end of June 2021 from 6.9 times at the end of December 2020 and has remained in compliance with its D/E ratio covenant of 10 times.

Asset quality to remain sound

ASK has managed its credit risk better than our previous expectation. We expect its sound asset quality to continue, thanks to prudent credit policies and efficient debt collection processes. The ratio of non-performing or stage-3 loans to total loans (NPL ratio) fell to 2.5% at the end of June 2021, from 2.9% at the end of 2020. The NPL formation ratio also fell, to 1.1% (annualized) in the first half of 2021 from 1.6% in 2020.

However, the company may still be impacted by the potential deterioration of asset quality resulting from the weak economy. Nonetheless, we estimate the NPL ratio will stay around 2.5% in 2021-2023 given the steady loan portfolio expansion. NPL formation is expected to increase slightly to 1.2%-1.3% in 2021-2023, while expected credit loss (ECL) should remain in the range of 1.3%-1.5% in 2021-2023.

The company anticipates that approximately 10% of its total loan portfolio may be potentially impacted after the end of the debt relief programs. These mainly include exposure in the service and tourism-related sectors. In response, ASK intends to build its ECL allowance to absorb any credit losses. We expect the company to maintain its conservative loan loss provisioning policies with an NPL coverage ratio at around its target of 100% during the next few years. At the end of June 2021, the company's NPL coverage ratio was 87%.

Earnings quality maintained

We expect ASK to sustain moderate profitability over the next few years, driven by effective management of its provision expenses, interest spread, and operating expenses. The company's earnings capability, measured by earnings before taxes to average risk-weighted assets (EBT/ARWA), was 2.6% (annualized) in the first half of 2021, up slightly from 2.5% in 2020. ASK reported net profit of THB545 million in the first six months of 2021, a 27% increase compared with the same period of the previous year. The higher net profit was mainly due to higher interest and non-interest income.

The company's recent diversification into higher-yielding auto title loans and working capital loans should partly compensate for the declining yields of auto loans. We estimate ASK's loan spread will be maintained in the range of 4.7%-4.9% over the next few years, from the current level of 4.9%. The company's focus on the insurance brokerage business after it received life insurance licenses also helped generate strong fee income in 2020 and the first half of 2021. This will likely continue to strengthen the company's non-interest income. In terms of costs, we expect operating costs to remain under control with the ratio of operating expenses to total income at 27% in the next few years as the company aims to enhance operating efficiency. Overall, we believe that the company should be able to sustain its EBT/ARWA in the range of 2.6%-2.7% over the next few years.

Funding and liquidity remain adequate despite some short-term debt obligations

The company's funding is assessed as adequate. Although it currently has some proportion of debt obligations that will mature within one year, we believe liquidity risk over the next 12 months remains manageable. At the end of June 2021, short-term obligations accounted for 46% of total debts. Of total maturing obligations within the next year, short-term debts make up 26%, while the current portion of long-term debts comprises 20%. The company intends to rely more on long-term proportions with a target funding structure of 80% long-term and 20% short-term.

At the end of August 2021, there were some mismatches in the maturities of ASK's assets and liabilities. Based on the company's estimates, loan repayments from customers over the next 12 months will total approximately THB15 billion while the company's loan repayment obligations will be approximately THB19 billion. However, ASK's back-up credit facilities from one of its shareholders, Bangkok Bank PLC (BBL), well-established relationships with financial institutions and ample credit facilities provide significant mitigants against liquidity risk that may arise in this uncertain environment. At the end of August 2021, the company had credit facilities totaling THB39.6 billion, 20% of which remained unused. However, some of the credit facilities from financial institutions are already secured by the company's hire-purchase receivables and the ability to secure additional credit facilities in the future may be limited. As of June 2021, the company's priority debt to total debt ratio was 33%.

Limited impact from COVID-19 on commercial truck loans

Thailand's total vehicle sales for the first eight months of 2021 increased by 2.4% year-on-year (y-o-y). Sales of commercial vehicles increased by 6.6%, in contrast with the sales of passenger cars which dropped by 5.4%. The lower impact on sales of commercial vehicles compared to passenger cars reflects the heightened demand for commercial vehicles due to increased logistics activities during the city lockdown. The number of new truck registrations also increased by 19% in the first eight months of 2021. Nonetheless, the overall impact on the auto industry combined with lending institutions' more stringent credit underwriting criteria caused outstanding loans of listed lenders to fall by 0.1% y-o-y in the first half of 2021, compared with a 1.9% growth in the first half of 2020. We expect economic recovery in 2022 to help improve performance

of both the auto manufacturers and the auto loan industry. The weakened asset quality in 2020-2021 is likely to be temporary and manageable.

BASE-CASE ASSUMPTIONS

TRIS Rating's base-case assumptions for ASK's performance in 2021-2023 are as follows:

- Loans to grow by around 18% in 2021 and expand by 9% annually thereafter.
- Loan spread to be maintained at 4.7%-4.9%.
- Expected credit loss to be around 1.3%-1.5%.

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 is premised on our expectations that capital and earnings capability will stay strong and asset quality will remain at an acceptable level.

RATING SENSITIVITIES

The rating and/or outlook upside hinges on ASK's ability to strengthen its market position significantly, while still maintaining acceptable loan quality and delivering satisfactory financial performance or improving its capital base with an RAC of more than 25%.

The rating and/or outlook could be revised downward should there be a significant deterioration in asset quality, with credit cost rising to more than 4%, which could adversely impact profitability. A downward revision could also occur if the company expands its loan portfolio aggressively resulting in the RAC dropping below 9%.

COMPANY OVERVIEW

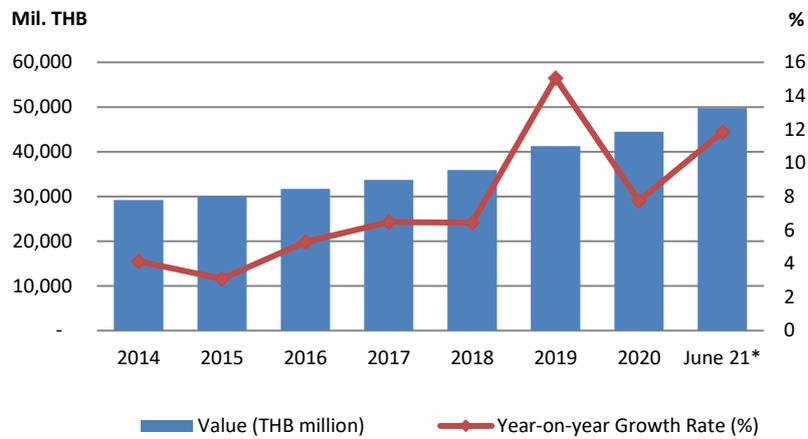
ASK was established by the Bangkok Bank Group (BBL Group) in 1984, as an auto hire-purchase lender. ASK subsequently became a wholly-owned subsidiary of Bangkok Grand Pacific Lease PLC (BGPL). BGPL, which concentrates on leasing loans for machinery and equipment (M&E) and factoring loans to corporate clients, was established in 1989 by the BBL Group and Chailease 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 50.4% stake in ASK. ASK is consolidated with Chailease Finance, based on the criteria of the power of control. Presently, the Chailease Group designates directors to ASK's board and supports ASK's liquidity needs. The BBL Group, holding an 11.6% stake in ASK, now supports ASK as a creditor rather than as an owner.

At the end of June 2021, approximately 78% 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 (15%) and other loans (7%).

KEY OPERATING PERFORMANCE

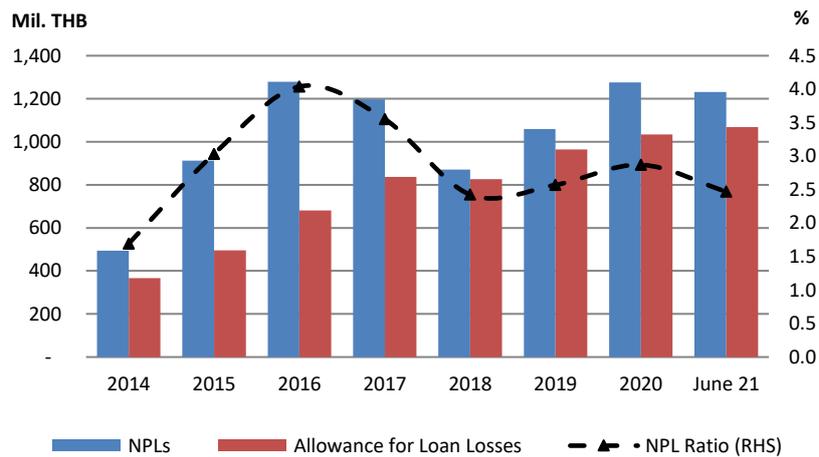
Chart 1: Outstanding Loans



Source: ASK

* Year-to-date growth for June-21

Chart 2: Asset Quality



Source: ASK's Financial Statement

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS*
Unit: Mil. THB

	Jan-Jun 2021	----- Year Ended 31 December -----			
		2020	2019	2018	2017
Total assets	50,397	44,931	41,815	36,252	33,999
Total loans	49,762	44,490	41,300	35,892	33,724
Allowance for expected credit loss	1,068	1,034	964	827	837
Short-term debts	18,621	20,609	24,128	18,200	17,178
Long-term debts	21,663	17,341	11,268	12,130	11,233
Shareholders' equity	8,596	5,668	5,424	5,121	4,831
Net interest income *	1,264	2,254	2,054	1,920	1,792
Expected credit loss	333	557	467	459	464
Non-interest income **	291	412	433	399	369
Operating expenses	540	988	945	859	777
Earnings before taxes	682	1,121	1,076	1,001	920
Net income	545	883	870	811	745

* Consolidated financial statements

Unit: %

	Jan-Jun 2021	----- Year Ended 31 December -----			
		2020	2019	2018	2017
Profitability					
Net interest income/average assets	5.30 **	5.20	5.26	5.47	5.46
Non-interest income/average assets	1.24 **	0.96	1.12	1.15	1.13
Operating expenses/total income	26.23	27.48	28.23	27.86	26.50
Operating profit/average assets	2.86 **	2.58	2.76	2.85	2.80
Earnings before taxes/average risk-weighted assets	2.63 **	2.49	2.69	2.79	2.74
Return on average assets	2.29 **	2.04	2.23	2.31	2.27
Return on average equity	15.29 **	15.92	16.49	16.30	15.84
Asset Quality					
Receivable in stage 3/total loans	2.47	2.87	2.57	2.43	3.55
Expected credit loss/average loans	1.41 **	1.30	1.21	1.32	1.42
Allowance for expected credit loss/receivable in stage 3	86.74	81.04	90.94	94.98	69.90
Capitalization					
Risk-adjusted capital ratio	15.10	12.06	12.59	13.84	13.95
Debt/equity (times)	4.88	6.93	6.71	6.08	6.04
Funding and Liquidity					
Stable funding ratio	95.31	73.39	65.57	78.95	79.94
Liquidity coverage measure (times)	0.02	0.02	0.02	0.01	0.02
Short-term debts/total liabilities	44.39	52.49	66.30	58.46	58.89

* Consolidated financial statements

** Annualized

RELATED CRITERIA

- Nonbank Financial Institution Methodology, 17 February 2020

Asia Sermkij Leasing PLC (ASK)

Company Rating:	BBB+
Rating Outlook:	Stable

TRIS Rating Co., Ltd.

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