

EASTERN COMMERCIAL LEASING PLC

No. 160/2022
22 September 2022

FINANCIAL INSTITUTIONS

Company Rating: BBB-
Outlook: Stable

Last Review Date: 27/09/21

Company Rating History:

Date	Rating	Outlook/Alert
10/09/20	BBB-	Negative
21/11/17	BBB-	Stable

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RATIONALE

TRIS Rating affirms the company rating on Eastern Commercial Leasing PLC (ECL) at “BBB-” and revises the rating outlook to “stable” from “negative”. The outlook revision reflects ECL’s improving trend in asset quality, financial leverage, and profitability. We expect the positive developments to continue over the next few years.

The rating also incorporates its relatively strong capital as well as adequate funding and liquidity. ECL’s moderate business position continues to weigh on the rating, despite our anticipation of the loan portfolio gradually expanding over the next few years. The uncertain economic environment and intense competition in the auto loan industry could also affect ECL’s asset quality if not well managed.

KEY RATING CONSIDERATIONS

Expect ECL to regain market position

ECL’s market position has gradually declined over the past few years. This is due to its conservative growth strategy driven by concerns over the risk of deteriorating asset quality. The company’s outstanding loans stood at THB4.2 billion at the end of June 2022.

We anticipate ECL to gradually regain its market position, supported by marketing efforts and collaborations with operators of major online used car e-commerce platforms to drive the growth of existing products. The company also plans to offer auto title loans as a new product to existing customers.

With its growth strategy, we expect ECL’s new loans to expand progressively. Based on our assumptions of around 20% growth per annum in 2022-2024, we estimate its outstanding loans to reach about THB5 billion by the end of 2024. We believe that used passenger car and high-engine-capacity motorcycle leasing sectors will continue to be its core businesses. In a short term, we expect ECL’s outstanding loan portfolio to contract by 22% in 2022.

Likely continued improvement in asset quality

Our outlook revision for ECL is based on asset quality improving steadily over the previous two years and our expectation that the company will be able to manage its asset quality while expanding its portfolio. The ratio of non-performing or stage-3 loans to total loans (NPL ratio) fell to 5.9% at the end of 2021 and 5.0% at the end of June 2022, from 8.3% at the end of 2020. Absolute NPLs fell to THB266 million at the end of 2021 from THB472 million at the end of 2020, with NPL formation turning negative.

However, with the portfolio expansion during an upturn in interest rate cycle and high inflation, ECL’s NPL formation in 2022-2024 could rise again. Nonetheless, the rise in NPLs should be manageable thanks to the company’s prudent credit underwriting policies and improved collection system. We estimate provisions for expected credit loss to average loans (credit cost) to be range between 1%-2% with NPL coverage ratio between 100%-130% in 2022-2024.

Cost efficiency, lower credit cost to support profitability

We expect the company to sustain moderate profitability over the next 2-3 years. The company’s earnings capability, measured by earnings before taxes to average risk-weighted assets (EBT/ARWA), improved progressively with

EBT/ARWA of 4.6% in 2021, up from 1.2% in 2020. For the first half of 2022, ECL's annualized EBT/ARWA ratio was 5.5%, with a net profit of THB104 million. We estimate ECL's EBT/ARWA to stay around 4.5%-4.6% during 2022-2024, which reflects its moderate profitability compared to peers.

In the medium term, the company is likely to maintain its interest spread while keeping its credit cost and operating expenses under control. After receiving the license for personal loans, the company will expand into higher-yielding auto title loans from 2022 onwards. Despite intense competition in the auto title loan segment that has led to falling loan yields, we expect its low funding cost to help maintain a spread of around 7%, while earnings should continue to strengthen in line with credit expansion. Meanwhile, the company's strategy to improve operating efficiency, efficiently utilize marketing budget, expand into online platforms, and outsource debt collection should help contain operating expenses under 40% of total income in 2022-2024.

Capital position to remain solid

Capital remains a key credit strength for ECL. At the end of June 2022, its risk-adjusted capital (RAC) ratio stood at 40.9%, while the debt to equity (D/E) ratio was at 1.47 times compared with its D/E ratio covenant of 4 times. In our view, there is ample room to support its additional debt-funded portfolio expansion in the medium term. Based on our expectation of moderate loan growth and dividend payout policy, we believe the current level of profitability will enable the company to maintain its strong capital position, with an RAC ratio in the range of 37%-41% over the next few years.

Adequate funding and liquidity profile

We assess the company's funding and liquidity profile as adequate. Although it currently has a high portion of debt obligations maturing within one year, we believe liquidity risk over the next 12 months remains manageable. At the end of June 2022, ECL's short-term obligations accounted for 70% of total borrowings. Of the total maturing obligations, long-term borrowings currently comprise 66%, and short-term borrowings comprise 34%.

We view ECL's well-established relationship with financial institutions and ample credit facilities as significant mitigants against liquidity risk that may arise in this uncertain environment. As of June 2022, the one-year liquidity gap was positive. Based on the company's estimates, loan repayments from customers over the next 12 months will be approximately THB2.3 billion and the company's loan repayment obligations will be approximately THB1.6 billion. At the end of June 2022, ECL held around THB1 billion in available credit facilities with financial institutions. The major shareholders have strengthened the company's relationship with financial institutions, helping to keep funding cost low and this will likely continue over the longer term. At the end of June 2022, ECL had outstanding bills of exchange (B/Es) of THB0.2 billion issued to major shareholders and THB0.5 billion guaranteed by Premium Group Co., Ltd. (Japan) (PG), representing 24% of total debts. Part of the credit facilities are secured by the company's hire-purchase receivables and ability to secure additional credit facilities in the future may be limited. As of June 2022, the company's priority debt to total debt ratio was 73%.

Outstanding auto loans improved following economic recovery

The Coronavirus Disease 2019 (COVID-19) pandemic has impacted the supply chain of the global automobile industry. Since 2021, the shortage crisis for automotive parts has affected car sales. As a result, used car prices improved. In the first half of 2022, the Bank of Thailand reported the used car price index at 113, up from 101 in 2021. We expect strong demand for automobiles to continue particularly as global economic recovery gathers momentum. Nonetheless, the higher inflation and the upward trend in interest rates may lead to delayed recovery in consumer purchasing power and deteriorating debt servicing ability. In our view, the deterioration in asset quality will likely pressure operators' profitability due to potential credit losses. Overall, we expect the growth of outstanding auto loans to improve in 2022. Outstanding loans of listed auto lenders increased by 2.4% year-to-date as of June 2022, compared with a 0.4% growth in 2021.

BASE-CASE ASSUMPTIONS

TRIS Rating's base-case assumptions for ECL's performance during 2022-2024 are as follows:

- New loans booked will expand by 20% per annum.
- Loan spread to be maintained at around 7.1%.
- Credit cost to range between 1%-2%.

RATING OUTLOOK

The "stable" outlook reflects the expectation that the company will be able to control its improved asset quality, continuously expand its portfolio to maintain market position, and deliver satisfactory financial performance.

RATING SENSITIVITIES

The rating outlook could be upgraded if the company significantly strengthens its market position with quality loan growth and strong capital and financial performance. The rating could be downgraded if the company’s asset quality deteriorates and/or operating performance weakens materially with EBT/ARWA falling below 1.5%.

COMPANY OVERVIEW

ECL was established by the Veerapong and Tantraporn families in 1984 and listed on the Stock Exchange of Thailand (SET) in 2004. Since it was established, ECL has focused on financing purchases of used automobiles through the hire-purchase loans and car loans or floor plan loans for vehicle dealers. As of June 2022, the Veerapong and Tantraporn families remained the largest shareholders, owning a combined 28% stake of ECL, followed by Premium Co., Ltd. (Premium), formerly known as Premium Financial Services Co., Ltd., with a 25.4% stake. PFS is a major originator of used auto financing and used car part warranty in Japan. The know-how and support from PFS have enabled ECL to improve operating efficiency and the debt collection system.

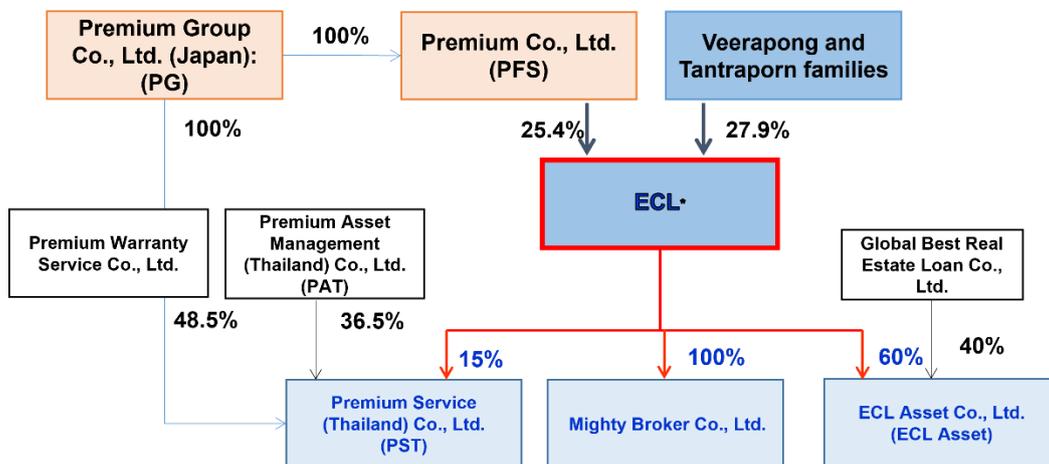
ECL is less geographically diversified than its competitors. The company offers services through its headquarters office and three branches, covering the Greater Bangkok area and the eastern region of Thailand.

In February 2018, ECL formed a new joint-venture company, ECL Asset Co., Ltd. (ECL Asset). ECL Asset is held by ECL (60%) and Global Best Real Estate Loan Co., Ltd. (40%). ECL Asset was formed as an operating business loaning to secure land properties on a registered mortgage or sale with the right of redemption basis as collateral. ECL started providing loans secured by land in the first quarter of 2018, a less liquid type of security compared with vehicles. TRIS Rating expects ECL to apply prudent underwriting criteria and expand conservatively. In November 2019, ECL entered the insurance broker business through the establishment and 100% ownership of Mighty Broker Co., Ltd.

However, ECL focuses on the used passenger vehicle and big bike segments, which are its primary areas of expertise. The loan portfolio at the end of June 2022 comprised mainly used passenger vehicles (56%) and big bikes (31%). The remaining 13% included pickup trucks, vans, commercial trucks, and others.

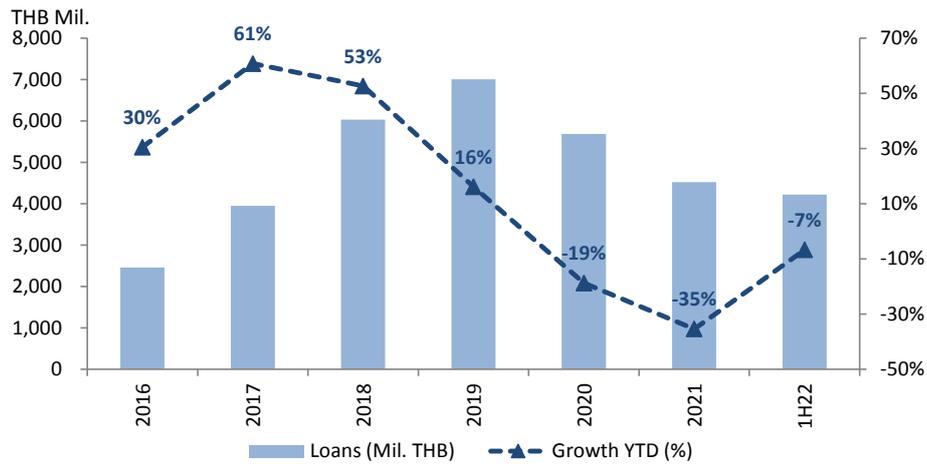
KEY OPERATING PERFORMANCE

Chart 1: ECL’s Group Structure as of Sep 2022



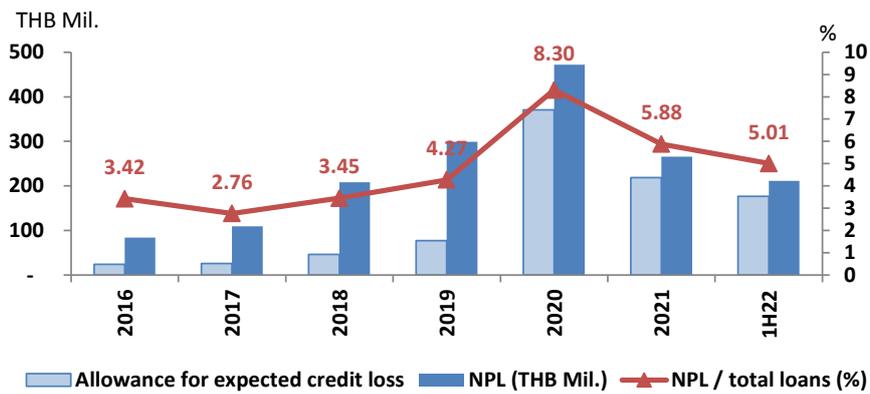
Source: ECL

Chart 2: ECL's Outstanding Loans



Source: ECL

Chart 3: NPLs, NPL Ratio, and Allowance for Expected Credit Loss



Sources: ECL's financial statements

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

	Jan-Jun 2022	Year Ended 31 December			
		2021	2020	2019	2018
Total assets	4,562	4,849	5,966	7,428	6,395
Total loans	4,217	4,523	5,687	7,002	6,028
Allowance for expected credit loss	177	219	371	77	46
Short-term debts	1,823	1,937	2,290	2,898	1,688
Long-term debts	814	1,018	1,862	2,539	2,832
Shareholders' equity	1,847	1,832	1,750	1,885	1,758
Net interest income	185	394	494	463	351
Expected credit loss	12	(23)	159	142	84
Non-interest income	77	161	191	232	191
Operating expenses	122	334	449	392	282
Earnings before taxes	127	244	77	160	176
Net income	104	194	62	130	142

* Consolidated financial statements

Unit: %

	Jan-Jun 2022	Year Ended 31 December			
		2021	2020	2019	2018
Profitability					
Net interest income/average assets	7.86 **	7.29	7.37	6.69	6.71
Non-interest income/average assets	3.27 **	2.66	2.85	3.35	3.65
Operating expenses/total income	38.96	48.40	49.85	42.54	40.28
Operating profit/average assets	5.41 **	4.51	1.15	2.32	3.36
Earnings before taxes/average risk-weighted assets	5.47 **	4.56	1.15	2.32	3.38
Return on average assets	4.40 **	3.59	0.92	1.88	2.72
Return on average equity	11.26 **	10.83	3.39	7.14	9.07
Asset Quality					
Receivable in stage 3/total loans	5.01	5.88	8.30	4.27	3.45
Expected credit loss/average loans	0.56 **	(0.44)	2.50	2.17	1.69
Allowance for expected credit loss/receivable in stage 3	83.57	82.37	78.52	25.79	22.22
Capitalization					
Risk-adjusted capital ratio	40.95	38.22	29.60	25.44	27.60
Debt/equity (times)	1.47	1.65	2.41	2.94	2.64
Funding and Liquidity					
Stable funding ratio	94.83	95.33	95.01	84.46	99.82
Liquidity coverage measure (times)	0.03	0.02	0.02	0.01	0.02
Short-term debts/total liabilities	67.15	64.20	54.31	52.29	36.41

** Annualized

RELATED CRITERIA

- Nonbank Financial Institution Methodology, 17 February 2020

Eastern Commercial Leasing PLC (ECL)

Company Rating:	BBB-
Rating Outlook:	Stable

TRIS Rating Co., Ltd.

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