TRIS RATING
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CreditNews ข่าวเครดิต

LEASE IT PLC

No. 197/2020
23 November 2020

FINANCIAL INSTITUTIONS

Company Rating: BBB-
Outlook: Negative

Last Review Date: 12/11/19

Company Rating History:

Date	Rating	Outlook/Alert
12/11/19	BBB-	Stable

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RATIONALE

TRIS Rating affirms the company rating on Lease IT PLC (LIT) at "BBB-" and, at the same time, revises the rating outlook to "negative" from "stable". The outlook revision reflects a material deterioration in the company's asset quality. The rating, however, continues to reflect the company's solid capital base and sufficient funding and liquidity. However, the rating is weighed down by LIT's modest market position and high credit concentration.

KEY RATING CONSIDERATIONS

Continuous deterioration in asset quality

Asset quality has been a key pressure point for the rating on LIT. Our revision of rating outlook to "negative" from "stable" reflects a significant deterioration of asset quality. The non-performing loan (NPL) ratio rose to 15.2% at the end of 2019 from the single-digit range in the past. The increase was mainly driven by its high credit concentration, with a number of large project financing loans involving lengthy court processes. At the end of first half 2020, the NPL ratio increased further to 22.7%. However, this was largely due to loan reclassification based on TFRS9 accounting standard, where all restructured loans were also classified as stage-3 (non-performing) loans. Excluding the TFRS9 impact, NPL ratio would have been at 19.5%. We note that the overall quality of the company's factoring business (34% of total as of June 2020) remains relatively healthy.

To manage its NPLs, the company has taken decision to write off NPLs that are in longer-than-expected litigation process. NPLs of THB112 million, 4.3% of average loans, were written off in the third quarter of 2020, compared with less than 1% charge-off rate in the past. Moreover, the company also tightens its credit policy and continues to reduce its exposure to the SMEs segment and high-risk industries.

We expect the acceleration of NPL write-offs and the tightening of credit policy to help improve its asset quality over the next few years. However, if there appears to be a deepened deterioration in asset quality, contrary to our expectation, the rating will be under incremental pressure.

Solid capital base

We expect LIT's capital to remain very strong in the medium term due to the slower pace of credit growth amid a weakening economy and the company's selective growth strategy. The company's capital strength measured by risk adjusted capital (RAC) ratio stood at 29.8% and 30.9% at the end of December 2019 and September 2020, respectively. Its robust capital that helps absorb credit losses that could potentially rise due to the economic fallout from the Coronavirus Disease 2019 (COVID-19) pandemic is a key factor supporting the company's credit profile.

Modest portfolio with high credit concentration

LIT's market position, measured by outstanding loans, is modest compared with other non-bank financial institutions (NBFIs) that we rate. Outstanding loans amounted to THB2.69 billion at the end of 2019, a 5.7% increase from the end of 2018. However, the outstanding loans contracted by 9.8% year-to-date at the end of September 2020 due to the impact from COVID-19. We expect the weak economic environment, coupled with the company's owned cautious growth strategy, could lead to further loan contraction in 2021.

Nonetheless, the loan contraction is unlikely to impact LIT's rating in the medium term as this is a similar trend seen for most NBFIs. The high credit concentration, on the other hand, has raised some concerns as it led to a steep rise in NPLs in recent years and has adversely impacted its financial performance. A gradual reduction in credit concentration would therefore alleviate the pressure on LIT's risk position. At the end of 2019, the top-20 customers accounted for 45% of outstanding loans.

Sufficient funding and adequate liquidity

We view that LIT should have sufficient funding to fund its business growth and continue to have a positive duration gap. In our view, the nature of LIT's short-term loans helps support its liquidity position better than lenders with longer term loans. In addition, LIT has access to funding from various sources including credit lines from domestic and foreign financial institutions, bills of exchange (B/E), and debentures.

LIT has a positive duration gap between its asset-liability structures. The average loan duration is between 3-6 months, while the average duration of borrowings is 15-18 months. In terms of funding structure as of September 2020, short-term borrowings accounted for 18.9% of total funding, long-term debt made up 37.7%, and the remaining 43.4% was equity.

The next debt repayment obligations for LIT include outstanding debentures of THB200 million due on 21 March 2021 and THB520 million due on 19 December 2021. We hold the view that the refinancing risk is manageable but note that the obligation due on 19 December 2021 is a major one, representing approximately 20% of total assets.

Loan loss reserves strengthened moderately

LIT has built up its loan loss reserves since the implementation of the TFRS9 accounting standard in 2020. The company set aside additional loan loss provisions of THB94.6 million via a reduction of retained earnings at the beginning of 2020. It also set aside additional provisions during the first half of 2020, resulting in allowance for loan loss increasing to THB391 million at the end of June 2020 from THB252 million at the end of 2019. Although loan loss reserves compared with outstanding loans rose materially to 15.34% at the end of June 2020 from 9.33% at the end of 2019, loan loss reserves to NPL (NPL coverage) improved only modestly to 67.6% from 61.5%. We are of the view that additional provisions through management overlays should help mitigate our concerns over the surging NPLs.

BASE-CASE ASSUMPTIONS

TRIS Rating's base-case assumptions for 2020-2022:

- New loans to shrink approximately by 20% in 2020 and grow around 10% per year thereafter.
- RAC ratio to remain above 30%.
- Overall interest yield to remain in the range of 10%-11%.
- Credit cost to remain at around 3%.
- Operating expense to total income ratio to stay between 30%-33%.

RATING OUTLOOK

The "negative" outlook reflects a material deterioration in LIT's asset quality. We expect the acceleration of NPL write-offs and the tightening of credit policy to help improve its asset quality over the next few years. However, if there appears to be a deepened deterioration in asset quality, contrary to our expectation, the rating will be under incremental pressure.

RATING SENSITIVITIES

The rating outlook could be revised to "stable" provided that the company's asset quality improves for a sustained period, while market position and financial performance are maintained.

The rating and/or outlook could be revised downward if the deterioration in asset quality prolongs and adds pressure on profitability as measured by earnings before taxes to average risk weighted assets, to the extent of the metric dropping below 1.5%. Additionally, an aggressive business expansion that causes the RAC ratio to drop below 25% would also trigger a rating downgrade.

COMPANY OVERVIEW

LIT was established in 2006 as Lease IT Co., Ltd., 99.99% owned by SVOA PLC (SVOA). LIT was initially established to act as a financial arm in providing leasing and hire purchase of SVOA's products to SVOA's customers. The company also provided factoring financing to help SVOA's customers on working capital management. In 2009-2010, the company started to diversify its business outside of SVOA's circle of customers and introduced other products such as trade finance, bid bond, and project back-up finance. In 2015-2016, the company introduced two more new products -- letter of credit (L/C) and supply chain finance.

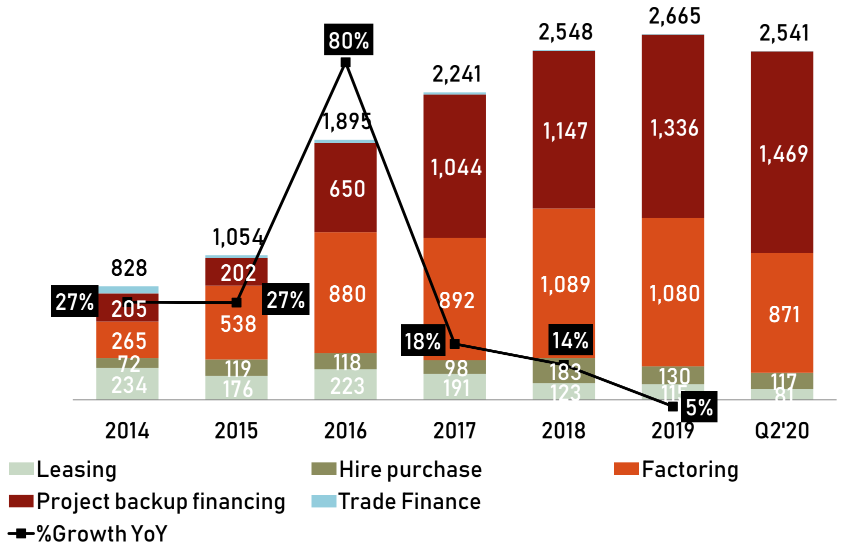
On 25 March 2014, LIT became a public company under the name “Lease IT Public Company Limited”. The company was subsequently listed on the “Market for Alternative Investment” (MAI), with THB200 million in registered and paid-up capitals. In 2017, the company offered to sell warrants (LIT-W1) to the company’s existing shareholders by way of a rights issue, totaling 160 million units of warrants at an offering price of THB2.5. The issue of the warrants enabled the company to increase its equity by THB400 million.

In May 2018, the company established a new subsidiary under the name “LIT Service Management Co., Ltd.” with registered share capital of THB5 million. The company’s principal business operations are providing data information and credit analysis services for Lease IT PLC. The subsidiary was established to segregate the roles between credit analysis and underwriter/approval.

KEY OPERATING PERFORMANCE

Chart 1: LIT’s Outstanding Loans

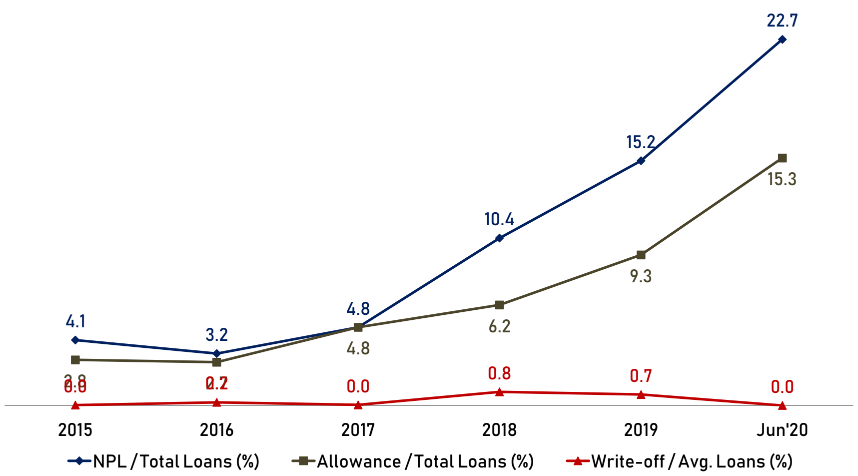
Unit: Mil. THB



Source: LIT

Chart 2: LIT’s NPL Ratio

Unit: %



Source: LIT

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS*

Unit: Mil. THB

		---------------- Year Ended 31 December			----------------
	Jan-Sep 2020	2019	2018	2017	2016
Total assets	2,608	3,551	2,663	2,346	1,992
Total loans	2,432	2,696	2,550	2,242	1,897
Allowance for doubtful accounts	282	252	159	109	51
Short-term borrowings	460	1,173	644	606	1,064
Long-term borrowings	918	1,109	734	556	332
Shareholders' equity	1,056	1,133	1,100	1,019	476
Net interest income	144	225	215	213	140
Non-interest income	95	148	161	144	102
Bad debts and doubtful accounts	47	111	71	58	24
Operating expenses	97	131	113	117	92
Net income	52	103	149	145	101

* *Consolidated financial statement*

Unit: %

		---------------- Year Ended 31 December			----------------
	Jan-Sep 2020	2019	2018	2017	2016
Profitability					
Net interest income/average assets	6.23 **	7.24	8.57	9.83	8.85
Net interest income/total income	47.11	49.24	48.23	50.87	48.75
Operating expenses/total income	31.86	28.63	25.48	27.94	31.92
Operating profit/average assets	4.06 **	4.23	7.66	8.36	8.01
Earnings before taxes/average risk-weighted assets	2.60 **	3.48	5.40	5.88	5.69
Return on average assets	2.25 **	3.32	5.94	6.71	6.36
Return on average equity	6.32 **	9.24	14.05	19.47	22.70
Asset Quality					
Non-performing loans***/total loans	16.74	10.38	10.38	4.84	3.22
Bad debts and doubtful accounts/average loans	2.47	4.21	2.94	2.83	1.61
Allowance for doubtful accounts/total loans	11.58	9.33	6.23	4.84	2.68
Capitalization					
Risk-adjusted capital ratio	30.92	29.75	29.31	30.42	16.78
Shareholders' equity/total loans	43.38	42.00	43.12	45.44	25.08
Debt/equity (times)	1.47	2.14	1.42	1.30	3.19
Liquidity					
Stable funding ratio	78.00	80.95	68.83	68.68	41.71
Liquidity coverage measure (times)	0.59	0.82	0.16	0.10	0.07
Short-term borrowings/total liabilities	29.66	48.49	41.22	45.68	70.22
Total loans/total assets	93.31	75.94	95.76	95.56	95.24
Total loans/short-term borrowings	528.49	229.96	395.71	369.76	230.06

* *Consolidated financial statement*
** *Annualized*
*** *Change definition in 2020 to staging from aging*

RELATED CRITERIA

- Nonbank Financial Institution Methodology, 17 February 2020

Company Rating:	BBB-
Rating Outlook:	Negative

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