

CHAYO GROUP PLC

No. 39/2022
25 March 2022

FINANCIAL INSTITUTIONS

Company Rating: BB+
Outlook: Stable

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RATIONALE

TRIS Rating assigns the company rating on Chayo Group PLC (CHAYO) at “BB+” with a “stable” outlook. The rating reflects the company’s extensive, long-standing experience and proven track record in managing unsecured distressed assets.

These strengths, however, are offset by its modest operating scale in comparison with other rated distressed asset managers. The rating also takes into consideration our expectation of the company’s rising financial leverage over the next few years given its aggressive acquisition plan for secured distressed assets. We also remain concerned over the uncertainty of CHAYO’s cash flows generated from divestments of non-performing assets (NPAs) during the next 12 months due to weak property demand.

KEY RATING CONSIDERATIONS

Focus shifted towards secured distressed assets

CHAYO is a distressed asset management company (DAMC) with extensive, long-standing experience and proven track record, particularly in debt collection services and managing unsecured distressed assets through wholly-owned Chayo Asset Management Co., Ltd. (Chayo AMC).

Over the past few years, CHAYO has shifted its focus to investments in secured distressed assets. The company recently established Chayo JV Co., Ltd. (Chayo JV), with THB920 million paid-up capital at the end of December 2021, to invest mainly in secured distressed assets. We view the establishment of Chayo JV as good strategy to further strengthen CHAYO’s market position and operating scale in the medium term. However, given the company’s short track record in managing secured distressed assets, success remains to be proven, in our view.

At the end of December 2021, secured distressed assets accounted for 66.6% of CHAYO’s gross distressed assets (loans to NPAs before accrued interest and impairment). We expect the figure to increase over the next few years given CHAYO’s current strategy to invest more in secured distressed assets.

Operating scale expanded but remains relatively modest

CHAYO has shown improvements in operating scale given its rapid growth in asset acquisitions particularly secured distressed assets in recent years. Its asset size expanded remarkably at a compound annual growth rate (CAGR) of 72.6% over the past three years, significantly outpacing the industry’s CAGR of 4.1% during the same period. However, CHAYO’s operating scale remains relatively modest. Its asset size of THB5.1 billion at the end of December 2021 represented a 2.01% market share among DAMCs in Thailand. While we expect the establishment of Chayo JV will help support its future growth, the current operating scale remains a rating constraint for CHAYO.

Increased NPL supply in the system provides growth opportunity

We expect non-performing loan (NPL) supply will increase over the next few years after the debt relief programs expire, which could provide opportunity for CHAYO and other DAMCs to acquire distressed assets at reasonable prices. Based on management’s strategy, CHAYO will expand its portfolio strongly over the next few years, through both Chayo AMC and Chayo JV. We project CHAYO’s asset size to expand substantially to THB9.4 billion by end-2024, mainly supported by the acquisition of secured distressed assets.

Expected increasing cash collection but uncertainty remains high

CHAYO's cash collection grew by 2% and 60.7% year-on-year (y-o-y) in 2020 and 2021, respectively. The growth was mainly supported by the sales of secured distressed assets (including NPLs secured by collaterals and foreclosed assets) acquired by the company over the past few years. However, its cash collection was below our expectation, disrupted by the city lockdown due to the Coronavirus Disease 2019 (COVID-19) pandemic in 2020-2021, weaker property demand, and a temporary closure of the Legal Execution Department, which essentially delayed legal processes.

We project an average growth of CHAYO's cash collection to be at 50% per annum during the next three years. The strong growth will be driven mainly by lumpy cash flows from sales of secured distressed assets acquired in recent years, despite our view of slow economic recovery and sluggish property demand in 2022. We expect the company's cash collection from secured distressed assets to account for around 75% of total cash collection on average over the next three years, compared with 53.3% in 2021. This is due to the company's shifted focus towards secured distressed assets in recent years.

That said, because of the greater portion of cash collection from secured distressed asset, the uncertainty of CHAYO's cash collection from distressed asset management business remains high during the next 12 months, in our view. This is because the disposal of secured distressed assets could be subject to various factors including legal processes, location, pricing, and demand. We also expect the adverse economic conditions caused by COVID-19 will continue to weigh on the company's overall business operations over the next 12 months.

Rising financial leverage during heavy investment phase

We believe CHAYO's aggressive investment strategy could put a strain on its financial profile in the coming years, despite a total capital increase of THB1.7 billion in 2021 upon exercise of its warrants (CHAYO-W1) and from the establishment of Chayo JV. Based on our projection, the capital will be used to invest mostly in distressed assets at the rate of THB2 billion per annum in 2022-2024. We estimate CHAYO's debt level to rise at a faster rate than its cash collection during the growth phase. This is because of the nature of managing secured distressed asset which is capital intensive and requires legal process that takes at least three years on average before each piece of asset could be disposed.

We expect the company's financial leverage, measured by adjusted debt to earnings before interest, taxes, depreciation, and amortization (adjusted debt/EBITDA) to rise substantially to 3.9 times and 4.2 times at the end of 2022 and 2023, respectively, from 0.4 times at the end of 2021. Our estimates incorporate our view that cash collection from sales of secured distressed assets could be delayed due to gradual economic recovery and lower property demand.

Sluggish revenue from debt collection services as the outbreak continues

CHAYO continued to report declining revenue of -22% y-o-y from debt collection services in 2021. This is mainly due to the extension of financial institutions' debt moratorium offered to their customers. We expect the company's revenue from debt collection services to remain sluggish in 2022 as relief programs have been extended at least until the end of 2022, according to the Bank of Thailand (BOT). We expect the revenues from debt collection services to recover back to pre-COVID-19 level in 2024 for both financial institutions and mobile network operators, which are major clients of CHAYO.

Adequate liquidity position

We view CHAYO's liquidity position as adequate, based on our expectations that sources of fund will still exceed uses of fund during the next 12 months. The sources of funds include estimated funds from operations (FFO) of around THB400 million during the next 12 months, cash on hand of THB1.3 billion at the end of 2021, debt refinancing, and THB100 million of expected undrawn credit facilities from financial institutions as of March 2022. Uses of funds consist of debt repayments totaling about THB328 million and planned distressed asset acquisition of about THB2 billion in 2022.

Portfolio concentration risk

CHAYO is subject to portfolio concentration risk as the top-10 investments in secured distressed assets accounted for around 40% of its total portfolio at the end of 2021. On a positive note, the figure declined from around 60% of its total portfolio at the end of 2020. However, the portfolio concentration risk is partially mitigated by the company's low acquisition cost compared with the appraised value of collateral and the appreciation of collateral value over time. Thus, the concentration risk is acceptable, in our view. Furthermore, we expect the portfolio concentration risk will gradually lessen to some extent as the overall distressed asset portfolio grows.

Distressed asset management continues to grow

The number of DAMCs has increased to 62 companies at the end of 2021 from 39 companies at the end of 2015. Aggregate assets of DAMCs have also expanded at a CAGR of 8.66% in 2016-2021. The severe impacts of the pandemic on the Thai economy resulted in a significant rise of NPLs of financial institutions (including Thai and foreign commercial banks and finance companies) to THB531 billion at the end of 2021 from THB465 billion at the end of 2019. While the asset warehousing

concept could lead to lower amount of distressed assets to be divested, we expect there are still vast opportunities for DAMCs to expand their assets.

BASE-CASE ASSUMPTIONS

Our base-case assumptions for CHAYO during 2022-2024 are as follow:

- Cash collection from unsecured distressed assets to range around THB300-THB380 million per annum.
- Revenues from debt collection service to range around THB42-THB64 million per annum.
- Gains on sales of foreclosed assets to range THB168-THB340 million per annum.
- Gross loans for loan offering business of around THB1.1-THB1.6 billion per annum.
- New acquisition of distressed assets of around THB2 billion per annum.

RATING OUTLOOK

The “stable” outlook reflects our expectation that CHAYO will continue to deliver satisfactory operating performance and strong cash collection growth over the medium term following its continuous distressed asset acquisition in recent years. Moreover, we also expect the company to maintain its financial leverage at an acceptable level.

RATING SENSITIVITIES

The rating and/or outlook upgrade could occur if the company is able to enlarge its cash flow from operation on a sustained basis, while maintaining its financial leverage at acceptable level. On the contrary, the rating and/or outlook could be revised downward if the company’s net debt to EBITDA ratio rises significantly above our expectation.

COMPANY OVERVIEW

CHAYO, initially named “Khien and Clay Co., Ltd.”, was established on 11 March 1997 with paid-up capital of THB3 million to operate debt tracking and collection service business. In accordance with the restructuring plan in 2015, the company changed its name to Chayo Group Co., Ltd. (CHAYO). CHAYO was listed on the Market for Alternative Investment (MAI) in February 2018. As of October 2020, the Yasasin family, the largest shareholder, held a 56.97% stake in CHAYO.

CHAYO now operates four main businesses including debt collection service business, distressed asset management business, lending business, and customer service business. The company has extensive experience in debt collection services before acquiring and managing its own distressed assets in 2014. In 2019, debt collection services generated around 20% of the company’s total revenue, while distressed asset management business accounted for around 80%.

CHAYO operates distressed asset management business through Chayo AMC, its wholly-owned subsidiary, who has the license granted from BOT under Emergency Decree on Asset Management Company B.E. 2541.

The company expanded into the lending business in 2018 after establishing its subsidiary “Chayo Capital Co., Ltd.” to provide both unsecured and secured loans. CHAYO holds 76% in Chayo Capital, and the remaining stakes are held by the Boonmechote family and Mr. Wiwat Kromadit.

CHAYO established Chayo JV with its partners to invest and/or jointly invest in asset management business and/or other relevant businesses in October 2020. CHAYO currently holds 55% voting power in Chayo JV.

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS
Unit: Mil. THB

	-----Year Ended 31 December -----				
	2021	2020	2019	2018	2017
Total operating revenues	806	520	318	265	207
Earnings before interest and taxes (EBIT)	381	248	149	112	88
Adjusted Earnings before interest, taxes, depreciation, and amortization (EBITDA)	445	295	190	140	142
Adjusted Funds from operations (FFO)	319	233	152	113	112
Interest expense	113	53	9	3	1
Capital expenditures	1,192	626	644	375	182
Total assets	5,090	2,811	1,825	829	415
Adjusted debt	1,494	1,604	585	36	56
Total equity	3,458	1,147	1,002	763	333
Adjusted Ratios					
EBITDA margin (%)	55.67	56.83	60.21	54.78	73.34
Pretax return on permanent capital (%)	9.81	11.44	12.50	18.88	26.36
EBITDA interest coverage (times)	3.94	5.59	20.71	48.86	120.50
Adjusted debt to EBITDA (times)	0.34	3.00	0.73	0.00	0.00
FFO to adjusted debt (%)	210.60	26.30	108.93	-	-
Adjusted debt to capitalization (%)	0.06	0.77	0.14	0.00	0.00

RELATED CRITERIA

- Key Financial Ratio and Adjustments for Corporate Issuers, 11 January 2022
- Rating Methodology – Corporate, 26 July 2019

Chayo Group PLC (CHAYO)

Company Rating:	BB+
Rating Outlook:	Stable

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