TRIS RATING
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NEXT CAPITAL PLC

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FINANCIAL INSTITUTIONS

Company Rating:	BBB-
Outlook:	Stable

RATIONALE

TRIS Rating assigns a company rating of "BBB-" to Next Capital PLC (NCAP) with a "stable" rating outlook. The rating reflects the company's solid capital base, sufficient funding, and adequate market position in motorcycle hire purchase (HP) lending. However, the key rating constraint is the potential weakness in asset quality of the company's motorcycle HP business. This is due to the high-risk credit profile of target customers whose debt serviceability could weaken amid fragile economic recovery and high inflation. The upcoming interest rate ceiling also remains a key challenge which may impact the company's profitability to an extent.

KEY RATING CONSIDERATIONS

Capital increase supports robust growth

A strong capital is one of NCAP's positive rating factors and likely to remain so in the medium term. Despite capital depletion in recent years given active credit expansion following its initial public offering (IPO) in 2020, we anticipate the company will continue its ambitious growth plan in the medium term. This will be supported by its recent rights offering (RO) that brought in an additional THB1.8 billion in capital in June 2022.

Following the RO, the company's capital as measured by the risk adjusted capital (RAC) ratio rose to 27.5% at the end of the second quarter of 2022 (2Q22), from 15.6% at the end of 1Q22. Even though the RAC ratio will gradually decline to about 19% by the end of 2024 owing to the company's growth plan, the company's capital position will continue to be assessed as strong. This is based on our assumption of robust growth in the company's outstanding loans of about 40% this year, 20% annually in 2023-2024, and a 40% dividend payout per year.

Improving market position

NCAP's market share in motorcycle HP measured by outstanding loans rose drastically to the third rank as of 1Q22 based on TRIS Rating's database from below top-five in 2020. This was owing to the company's strong loan growth in recent years against a gradual loan contraction for its peers, most of which have remained cautious since the start of the Coronavirus Disease 2019 (COVID-19) pandemic.

NCAP's loan portfolio reached THB7.8 billion at the end of 2Q22 from THB4.0 billion at the end of 2020. Given our assumptions on the growth rate of NCAP's outstanding loans, we expect its loan portfolio to reach THB10 billion by the end of 2023. The ability to sustain robust growth and maintain market position in the longer term without compromising capital and asset quality may have a positive impact on its rating.

As for business diversity, NCAP has relatively good geographic diversification, with a branch network across diverse regions of Thailand. In 1Q22, the company's loan portfolio underwritten in Bangkok, the southern, northern, northeastern, and other regions accounted for 21%, 27%, 17%, 16%, and 19% of total loan portfolio, respectively.

Sufficient funding support and liquidity

NCAP has adequate funding and liquidity for its business expansion. As a listed company, it has strong and diverse credit relationship with various financial

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institutions. The company also receives financial support from its two largest shareholders, COM7 PLC (COM7) and Synnex (Thailand) PLC (SYNEX) in the forms of revolving credit lines. At the end of June 2022, its total outstanding credit lines with financial institutions amounted to THB3.9 billion. Additionally, outstanding short-term loans provided by COM7 and SYNEX totaling THB1.0 billion in 1Q22 were repaid in 2Q22 using the capital received from the RO.

The company has high portion of long-term funding, representing 79% of its capital structure, of which 27.5% were long-term borrowings and 51.5% was equity as of June 2022. At the end of June 2022, short-term obligations accounted for 43% of its total borrowings. The company estimates cash inflows from customer loan repayments to amount at around THB160-THB180 million per month over the next 12 months, which are sufficient for monthly loan servicing. We believe the current cash inflows plus ample credit lines from financial institutions and parent companies should provide adequate funding and liquidity for the company's future growth.

Asset quality remains a challenge amidst an uncertain environment

Although the company's overall asset quality appears sound and manageable compared with peers, the recent deterioration in the non-performing loan (NPL) ratio, which rose to 1.95% at the end of 2Q22 from 1.35% at the end of 2021, confirms our belief that NCAP remains under pressure from the weak economy and rising inflation given the high-risk credit profile of its target customers. Its ambitious growth targets combined with fierce competition in the motorcycle HP segment could create additional pressure on asset quality if loan underwriting is not well controlled. The inherent risk associated with the company's target customers is a key rating constraint, in our view.

In terms of provisioning, despite the low NPL ratio, NCAP maintains a high level of credit cost (provisions for expected credit loss (ECL) to average loans), similar to its direct peers. In the first half of 2022, the company's credit cost was 11.7% (annualized), increasing from 9.9% (annualized) in 1Q22 and 7.5% in 2021. The rise in credit cost followed the deterioration in the company's asset quality in 2Q22 reflected by higher under-performing loans (stage 2) and NPLs (stage 3). Additionally, the ECL of performing loans (stage 1) continued to rise, which suggests signs of asset quality deterioration given the company's strong growth. The allowance for ECL to total loans increased to 6.6% in 2Q22, from 5.4% at the end of 2021. Should asset quality continue to deteriorate significantly, NCAP's credit cost could rise from the current level, affecting the company's profitability.

High competition and interest rate ceiling could impact loan growth and profitability

Motorcycle sales and leasing recovered moderately in 2021, following the economic fallout from COVID-19 that caused motorcycle sales and HP loans to fall by 11.8% and 1.7%, respectively, in 2020. In 2021, motorcycle sales grew by 6% year-on-year (y-o-y), while loan growth for the eight largest operators in our database was flat. Although demand for motorcycles remains strong this year, supply shortages caused sales to grow by only 3% y-o-y in the first five months of 2022. On the lending side, tightened loan approvals due to weaker customer credit profiles have contributed to the slowdown in lending as well.

Moreover, several new players have entered the market because of the still-high loan yield compared with other types of consumer lending, leading to heightened competition in the motorcycle segment. That said, to help protect consumers, the regulator is pushing for an interest rate cap on motorcycle HP loans. The new regulation that is soon to be announced is likely to cap the interest rate at not more than 30%. This could put additional pressure on the loan growth and profitability of the motorcycle HP lenders.

BASE-CASE ASSUMPTIONS

TRIS Rating's base-case assumptions for 2022-2024 are:

- Outstanding loan portfolio to grow over 40% in 2022 and expand by around 20% per year in 2023-2024.
- RAC ratio to remain around 25% in 2022 and around 20% in 2023-2024.
- Loan yield to remain around 21%.
- Credit cost to be around 9%.
- Operating expense to total income ratio to be around 39%.

RATING OUTLOOK

The "stable" outlook is based on our expectation that NCAP will expand its portfolio continuously to maintain its leading market position, with satisfactory financial performance, asset quality, and leverage.

RATING SENSITIVITIES

The rating and/or outlook upside hinges on NCAP's ability to continue to improve its market position while maintaining its asset quality, financial performance, and solid capital base. The rating and/or outlook could be revised downward should asset quality deteriorate continuously or due to aggressive loan portfolio expansion, which would affect profitability with EBT/ARWA below 1.5% or an RAC ratio below 15% on a sustained basis.

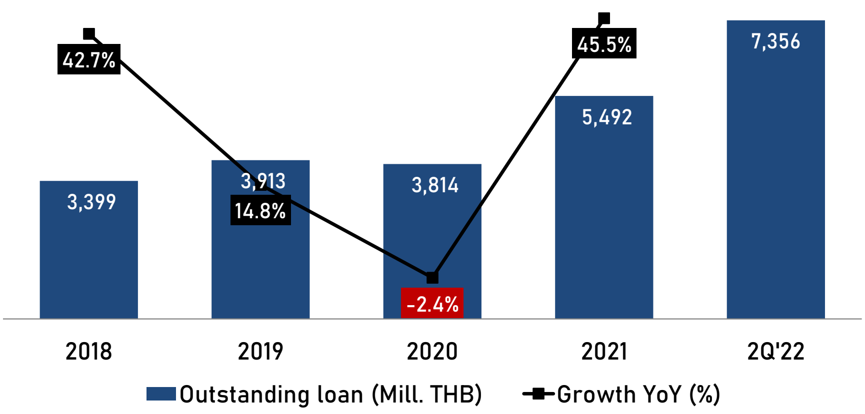
COMPANY OVERVIEW

NCAP was established on 17 August 2004 with registered capital of THB8 million under the name BAF (Thailand) Co., Ltd. by Mitsui & Co., Ltd., a company in the Mitsui Group Japan. The company provided HP loans exclusively for Yamaha motorcycles (captive finance). In 2014, the company began expanding the scope of its business, providing loans for the HP of motorcycles under other brands, such as Honda, Vespa, Kawasaki, and Suzuki.
In 2017, Mitsui Group Japan reduced its shareholding to 25% of the company's registered capital and, in 2019, sold all its remaining shares. The major shareholders of the company as of the end of 2019 were COM7 and SYNEX which each held shares of 40% of the THB300-million paid-up registered capital. The company became public company in March 2020 and the registered capital was increased to THB450 million. Shares were offered to the public through an IPO in November 2020. The major shareholders of the company as of the end of 2020 were COM7 and SYNEX, holding 33.93% and 26.67% of the paid-up registered capital, respectively.

NCAP operates the HP lending business, focusing on retail customers seeking to buy new motorcycles. The company reaches its customers via local dealers who are the company's business partners. The company offers the services across all regions of Thailand with the southern region being the largest market followed by Bangkok and the northern region.

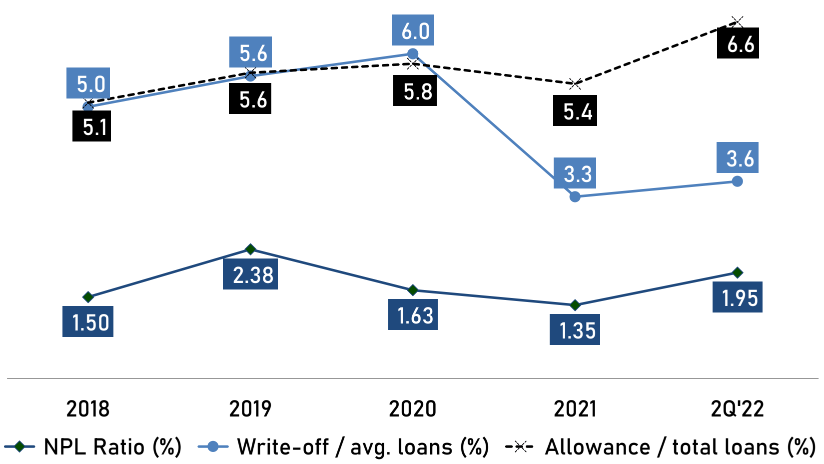
KEY OPERATING PERFORMANCE

Chart 1: Outstanding Loans



Source: NCAP

Chart 2: Asset Quality



Source: NCAP

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS*

Unit: Mil. THB

	Jan-Jun 2022	---- Year Ended 31 December ---- 2021	2020	2019	2018
Total assets	8,427	5,831	4,657	4,076	3,566
Total loans**	7,817	5,777	3,970	4,067	3,545
Allowance for expected credit loss	513	314	230	229	180
Short-term debts	1,709	1,141	1,141	2,270	1,200
Long-term debts	2,240	2,207	1,624	605	1,304
Shareholders' equity	4,138	2,008	1,676	1,053	926
Net interest income	656	931	766	759	622
Expected credit loss	399	363	379	368	209
Non-interest income	207	350	268	132	27
Operating expenses	366	528	403	362	324
Earnings before taxes	99	389	253	162	116
Net income	78	311	202	126	90

* *Consolidated financial statements*
** *Include deferred commission expense*

Unit: %

	Jan-Jun 2022	---- Year Ended 31 December ---- 2021	2020	2019	2018
Profitability					
Net interest income/average assets	18.42 **	17.75	17.55	19.87	20.57
Non-interest income/average assets	5.80 **	6.67	6.15	3.46	0.89
Operating expenses/total income	38.80	38.31	35.13	35.68	43.78
Operating profit/average assets	2.78 **	7.43	5.79	4.23	3.83
Earnings before taxes/average risk-weighted assets	1.51 **	3.76	3.24	2.18	1.97
Return on average assets	2.20 **	5.93	4.62	3.30	2.98
Return on average equity	5.09 **	15.86	14.78	12.76	12.27
Asset Quality					
Non-performing loans/total loans	1.95	1.35	1.63	2.38	1.50
Expected credit loss/average loans	11.73 **	7.46	9.42	9.67	6.95
Allowance for expected credit loss/non-performing loans	336.97	402.00	356.69	236.79	339.12
Capitalization					
Risk-adjusted capital ratio	27.54	17.90	21.78	13.32	13.38
Debt/equity (time)	1.04	1.90	1.78	2.87	2.85
Liquidity					
Stable funding ratio	136.80	116.23	161.00	73.25	115.41
Liquidity coverage measure (times)	0.42	0.07	0.62	0.00	0.01
Short-term debts/total liabilities	39.85	29.85	38.27	75.10	45.45

* *Consolidated financial statements*
** *Annualized*

RELATED CRITERIA

- Nonbank Financial Institution Methodology, 17 February 2020

Next Capital PLC (NCAP)

Company Rating:	BBB-
Rating Outlook:	Stable

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