

ASIA SERMKIJ LEASING PLC

No. 166/2019
15 October 2019

FINANCIAL INSTITUTIONS

Company Rating: BBB+
Outlook: Stable

Last Review Date: 10/10/18

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” outlook. The rating reflects ASK’s moderate and steady credit growth, asset quality improvement, and acceptable operating results, as well as the business support and financial support it receives from its major shareholders. The rating also takes into account the company’s moderate capital level and relatively high financial leverage.

The key rating concerns is downward pressure on profitability due to intense competition. Its target customers, which are mainly small- and -medium sized operators in the commercial vehicle segment, are especially vulnerable to economic downturns.

KEY RATING CONSIDERATIONS

Moderate business growth

The company continues to enhance its market position gradually, as shown by the steady growth in its loan portfolio over the last few years, in line with major peers in the industry. During 2014-2018, new loans expanded by 7% on average, while the company’s outstanding loan portfolio grew by approximately 6% per year. At the end of June 2019, outstanding loans had increased to Bt38.3 billion, a 6.7% year-to-date rise as a result of expanding market coverage, cross, and expansion in to high-yield lending.

TRIS Rating projects ASK’s consolidated loan portfolio will expand gradually with an annual growth rate above 6% over the next three years. We believe that auto financing loans will continue to provide the major growth impetus, especially in its core business, the truck segment. At the end of June 2019, ASK’s outstanding retail auto loans comprised loans for big trucks, accounting for 60% of its loan portfolio, and loans pickup cars and passenger cars accounting for the remainder. Other growth drivers are auto title loans and inventory financing, which generates interest yields of around 10% -12%, higher than auto loans that generate 7%-8% yields.

Strengthened asset quality and reserves

The rating is based on our expectation that asset quality will remain sound, with the ratio of non-performing loans (NPLs) to total loans staying below 3% in the next three years, assuming a credit cost of around 1% in 2019-2021. This will be supported by the more stringent underwriting loan standards, and an efficient collection system.

ASK has improved its loan quality continuously. The NPL ratio declined to 2.3% at the end of June 2019 from 2.4% at the end of 2018. ASK focuses on specific sub-segments of asset types and customer groups that are less risky in order to mitigate the higher risk from loans for commercial vehicles, which although generating higher returns often come with higher credit risk.

ASK’s NPL coverage in the past has been weaker than peers but has now strengthened to be more in line with the industry average. The coverage ratio rose steadily to 97.7% at the end of June 2019 from 53.2% at the end of 2017. We expect the coverage ratio to remain at least at the current level as the company prepares for the implementation of IFRS 9 in 2020.

Challenge to steady profitability

We forecast ASK's return on average assets (ROAA) will remain above 2.5% in 2019-2021, assuming a credit cost of about 1% and average operating expenses to total income of 29%. In 2018, net income grew by 9% to Bt811 million from 2017, despite an increase in operating expenses of 10% over the same period. The increase in net income was a combination of a 6% increase in net interest income, 15% rise in non-interest income, and a reverse in provision expenses. However, we expect credit costs in 2019-2021 may be lower than the past due to improved asset quality.

In terms of loan yields, we expect ASK to maintain an interest rate spread in the 4.7%-5.0% range in 2019-2021. The intense competition in the commercial vehicle segment, which has resulted in decreasing yields, will pose challenges to the company's profitability. Nonetheless, ASK aims to enhance yields by expanding into auto title loans and inventory financing, which can generate higher yields than the auto loans.

Financial support from major shareholders to mitigate liquidity risk

There are some mismatches in the maturities of ASK's assets and liabilities because during the past few years, the company has used short-term borrowings in an attempt to keep its funding costs low. At the end of June 2019, short-term borrowings, including the current portion of long-term borrowings, accounted for approximately 60% of total borrowings. We note that the short-term funding instruments carry refinancing risks. Nevertheless, TRIS Rating expects ASK's back-up credit facilities from one of its shareholders, Bangkok Bank PLC (BBL), and other financial institutions will be sufficient to cover the outstanding short-term funding instruments it has issued through the capital markets.

Capital base remains moderate

ASK's capitalization is considered moderate compared with its rated peers. Its capital level is appropriate for the current rating and sufficient to support the company's expansion plan in the medium term.

ASK has remained in compliance with its debt to equity (D/E) covenant of 10 times. Its current D/E ratio of 6.8 times at the end of June 2019 is appropriate with the current rating. However, an increase in the D/E ratio could eventually put pressure on the rating and/or outlook. Given our expectation of moderate loan growth of approximately 6% annually during the next three years, we expect ASK to remain in compliance with the debt covenants even as it continues to expand. However, if growth exceeds our forecast, an increase in capital may be needed to bolster the capital base.

BASE-CASE ASSUMPTIONS

- Outstanding loans to expand by an average of 6% per annum in 2019-2021
- Loan spread to be maintained at 4.7%-5.0% in 2019-2021
- Credit cost to be around 1.0% in 2019-2021

RATING OUTLOOK

The "stable" outlook is based on TRIS Rating's expectation that ASK will be able to maintain its market positions in the chosen niche markets for commercial vehicles. The outlook also factors in our expectation that ASK will maintain efficient risk management and operating systems to ensure that loan quality is preserved at the current level or improves further. The outlook also takes into account stable profitability and on-going support from its major shareholders.

RATING SENSITIVITIES

The rating and/or outlook upside hinges on ASK's ability to strengthen its market position significantly, with steady loan quality, satisfactory financial performance, and a solid capital base with D/E less than 4.5 times.

The rating and/or outlook could be revised downward should ASK's market position weaken materially, or if the company funds its growth by relying heavily on debt with D/E more than 8 times. A significant deterioration in the NPL ratio or an interest spread below our expectation could adversely impact profitability and pressure the rating.

COMPANY OVERVIEW

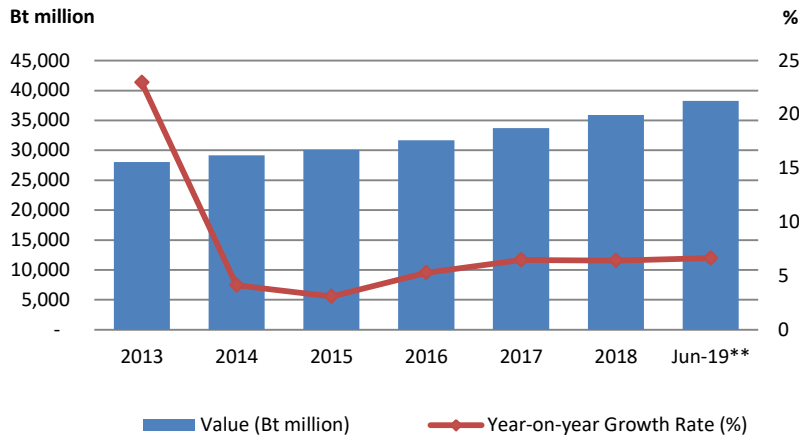
ASK was established by the Bangkok Bank Group (BBL Group) in 1984, as an auto hire-purchase lender. ASK subsequently became a wholly-owned subsidiary of Bangkok Grand Pacific Lease PLC (BGPL). BGPL, which concentrates on leasing loans for machinery and equipment (M&E) and factoring loans to corporate clients, was established in 1989 by the BBL Group and Chalease 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 48.18% stake in ASK through two subsidiaries: Chailease Finance Co., Ltd., holding 36.61%, and Chailease International (Malaysia) Co., Ltd., holding 11.57%. ASK is consolidated with Chailease Finance, based on the criteria of the power of control. Presently, the Chailease Group designates six directors to ASK's board and supports ASK's liquidity needs. The BBL Group, whose shareholding was diluted after the 1997 financial crisis, now supports ASK as a creditor rather than as an owner.

At the end of June 2019, approximately 83% 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 (13%) and other loans (4%).

KEY OPERATING PERFORMANCE

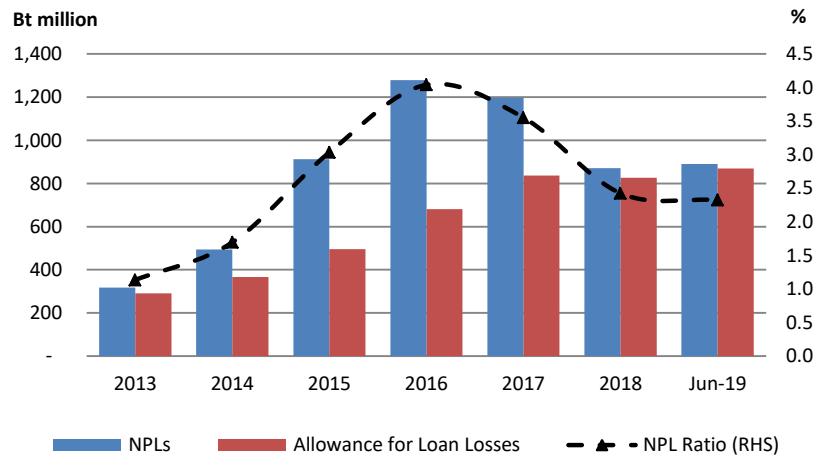
Chart 1: Outstanding Loans



Source: ASK

* Year-to-date growth for Jun-19

Chart 2: Asset Quality



Source: ASK

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS*
Unit: Bt million

	Jan-Jun 2019	----- Year Ended 31 December -----			
		2018	2017	2016	2015
Total assets	38,539	36,252	33,999	31,707	30,249
Total loans	38,280	35,892	33,724	31,671	30,079
Allowance for doubtful accounts	870	827	837	681	495
Short-term borrowings	21,755	18,200	17,178	16,576	17,103
Long-term borrowings	10,787	12,024	11,139	9,773	8,098
Shareholders' equity	4,958	5,121	4,831	4,578	4,347
Net interest income	974	1,894	1,792	1,660	1,516
Bad debts and doubtful accounts	215	459	464	380	270
Non-interest income	219	425	369	326	302
Operating expenses	481	859	777	738	694
Net income	403	811	745	707	681

* Consolidated financial statements

Unit: %

	Jan-Jun 2019	----- Year Ended 31 December -----			
		2018	2017	2016	2015
Profitability					
Net-interest income/average assets	5.21 **	5.39	5.46	5.36	5.08
Net-interest income/total income	60.77	61.44	61.09	58.94	55.71
Operating expenses/total income	30.00	27.86	26.50	26.20	25.51
Operating profit/average assets	2.66 **	2.85	2.80	2.80	2.86
Return on average assets	2.16 **	2.31	2.27	2.28	2.28
Return on average equity	16.01 **	16.30	15.84	15.84	16.07
Asset Quality					
Non-performing loans/total loans	2.33	2.43	3.55	4.04	3.03
Bad debts and doubtful accounts/average loans	1.16 **	1.32	1.42	1.23	0.91
Allowance for doubtful accounts/total loans	2.27	2.30	2.48	2.15	1.65
Allowance for doubtful accounts/non-performing loans	97.72	94.98	69.90	53.19	54.22
Capitalization					
Shareholders' equity/total assets	12.86	14.13	14.21	14.44	14.37
Shareholders' equity/total loans	12.95	14.27	14.32	14.46	14.45
Debt to equity (time)	6.77	6.08	6.04	5.93	5.96
Liquidity					
Short-term borrowings/total liabilities	64.78	58.46	58.89	61.10	66.03
Total loans/total assets	99.33	99.01	99.19	99.89	99.44

* Consolidated financial statements

** Annualized

RELATED CRITERIA

- Nonbank Lending Company, 7 May 2018

Asia Sermkij Leasing PLC (ASK)

Company Rating:	BBB+
Rating Outlook:	Stable

TRIS Rating Co., Ltd.

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