

EASTERN COMMERCIAL LEASING PLC

No. 185/2022
28 September 2023

FINANCIAL INSTITUTIONS

Company Rating: BBB-
Outlook: Stable

Last Review Date: 22/09/22

Company Rating History:

Date	Rating	Outlook/Alert
22/09/22	BBB-	Stable
10/09/20	BBB-	Negative
21/11/17	BBB-	Stable

Contacts:

Siriwan Weeramethachai
siriwan@trisrating.com

Sithakarn Tongphiphat, CFA, FRM
sithakarn@trisrating.com

Jittrapan Pantaleard
jittrapan@trisrating.com

Taweekok Jiamsakunthum
taweekok@trisrating.com

Narumol Charnchanavivat
narumol@trisrating.com



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RATIONALE

TRIS Rating affirms the company rating on Eastern Commercial Leasing PLC (ECL) at “BBB-” with a “stable” outlook. The rating reflects primarily the company’s strong capital base, and adequate funding and liquidity.

However, the strengths are weighed down by ECL’s moderate business position and the weakening of earnings capacity caused by higher funding costs and pressure on loan yields amid intense competition. Other constraints include a potential rise in credit risk due to the weak economy.

KEY RATING CONSIDERATIONS

Solid capital position

ECL’s very strong capital base is the key supporting factor for the rating. The company’s capital, measured by the risk adjusted capital (RAC) ratio, stood at 39.7% at the end of June 2023. Its financial leverage, measured by the debt to equity (D/E) ratio, was 1.5 times, compared with the D/E ratio covenant on its debt obligations of 4 times.

We continue to assess the company’s capital position as very strong, even though the RAC ratio is likely to gradually decline owing to the company’s growth plan. We estimate its RAC ratio to be in the range of 30%-38% in 2023-2025. This is based on our assumption that the company’s outstanding loans will expand by about 13% in 2023 and 16%-17% in 2024-2025, with a 60% dividend payout per year.

Gradual portfolio expansion supports business position

ECL has expanded its loan portfolio gradually starting in the third quarter of 2022 (3Q22) after a steady decline since 2019. We expect the credit expansion to help secure the company’s market position. Outstanding loans increased by 8% year-to-date to THB4.6 billion at the end of June 2023. We expect outstanding loans to gradually increase, supported mainly by its active marketing strategy for its core business, in the used passenger car and high-engine-capacity motorcycle leasing.

ECL has also introduced new products including title loans for its existing clients and solar rooftop loans which are still in a small operating scale. We expect outstanding loans for the two products to reach around THB50-THB100 million in 2023-2025. In the longer term, if the expansion continues, we believe diversification should help support ongoing business growth and alleviate pressure on loan yields, supported by the mix of higher yields from title loans.

Asset quality remains manageable

ECL has improved its asset quality significantly over the past few years. We expect its asset quality to remain sound despite some deterioration in recent quarters. Asset quality is supported by the company’s cautious growth strategy and more efficient collection system. The ratio of stage-3 loans (NPLs) fell to 4.2% at the end of June 2023 from 4.7% at the end of 2022.

NPL formation also decreased notably from the peak of THB202 million in 2019 (3.1% of average loans) to THB15 million in the first half of 2023 (1H23) or 0.7% of average loans. Despite the weak credit environment, we expect NPL formation to remain below 2% in 2023-2025.

In terms of provisioning, the company raised its expected credit loss (ECL) provisions to average loans or credit cost to 1.4% (annualized) in 1H23, from 0.7% in 2022, to absorb larger credit losses in the commercial segment. For passenger cars and high-engine capacity motorcycle (big bikes), loan loss provisions have declined in line with improved asset quality.

NPLs may continue rising over the next few years if the company expands its business more actively in an environment of intense competition and still-weak economic conditions. Nonetheless, the rise in credit cost should be manageable, supported by more prudent loan approvals and efficient debt collections. TRIS Rating expects the company's credit cost to be in the range of 1%-2% in 2023-2025. With our assumption of higher NPL write-offs of 1.2% to average loans in 2023-2025, the NPL ratio is likely to stay within 3%-4%. As of June 2023, NPL coverage stood at 91%. We expect NPL coverage to rise to the range of 95%-110%.

Higher costs pressure earnings

We expect ECL to maintain earnings capacity in the "moderate" range over the next 2-3 years despite potentially weaker earnings. ECL's earnings capacity, as measured by earnings before taxes to average risk-weighted assets (EBT/ARWA), decreased to 3.9% (annualized) in 1H23, from 5.0% in 2022. In our base-case assumptions, we expect EBT/ARWA to be around 3% in 2023-2025, which still supports the current rating. This is based on our estimated spread around 4%, lower than about 6% in 2020-2022 due to elevated funding cost.

In 1H23, ECL reported net profit of THB72 million, a 31% decrease year-on-year (y-o-y). The decline was caused by higher credit costs, operating expenses from marketing activities, and staff costs. The ratio of operating expenses to total income increased to 45% in 1H23, from 41% in 2022. An improvement in operating efficiency to help contain the rise in operating expenses in the range of 43%-44% of total income in 2023-2025.

Funding and liquidity remain adequate

In terms of funding structure, we view that there is maturity mismatch between assets and liabilities to some extent as ECL has relied on short-term borrowings to keep funding costs low, while its assets are mostly long-term. At the end of June 2023, short-term obligations accounted for 31% of total debts, increasing from 12%-18% in the past few years. Of total short-term debt, 29% or THB200 million was in the form of bills of exchange (B/Es) issued to major shareholders while THB600 million was guaranteed by its ultimate major shareholder, Premium Group Co., Ltd. (Japan) (PG).

As for liquidity, we expect the company to be able to refinance its short-term borrowings given its well-established relationships with financial institutions and funding support from major shareholders. At the end of June 2023, based on the company's estimates, customer loan repayments should reach THB170-THB200 million per month over the next 12 months (September 2023 – August 2024), which would be sufficient for monthly loan servicing. Moreover, ECL's ample back-up credit facilities from financial institutions should help mitigate liquidity risk. At the end of June 2023, the company had credit facilities totaling THB5.3 billion, 15% of which remained unused.

ECL's priority debt ratio is considered high. As of June 2023, the company's priority debt to total debt ratio was 76%. This is due to the requirement for most of its bank borrowings to be secured by receivables, which implies that ECL's ability to secure additional credit facilities in the future could be limited in a stress scenario. The high priority debt ratio suggests a significant subordination risk for the company's unsecured obligations, according to TRIS Rating's "Issue Rating Criteria".

BASE-CASE ASSUMPTIONS

TRIS Rating's base-case assumptions for ECL's performance during 2023-2025 are as follows:

- Outstanding loans to expand by 13% in 2023 and 16%-17% in 2024-2025.
- Spread to be maintained at around 4%.
- Credit cost to range from 1.5%-1.7%.
- Operating expenses to total income to range from 43%-44%.

RATING OUTLOOK

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

RATING SENSITIVITIES

The rating outlook could be revised upward 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% for an extended period.

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. Know-how and support from PFS have enabled ECL to improve operating efficiency and the debt collection system.

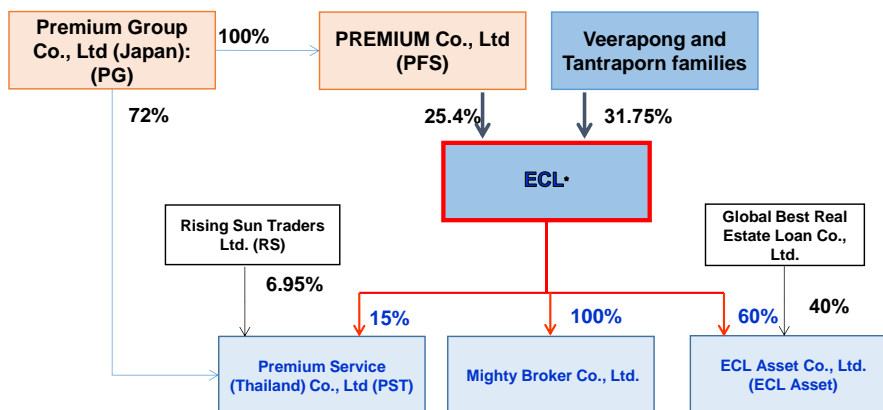
ECL is less geographically diversified than its competitors. The company offers services through its headquarters office and four branches, covering the Greater Bangkok area and the eastern region of Thailand.

In February 2018, ECL formed a joint-venture company, ECL Asset Co., Ltd. (ECL Asset), which 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 brokerage 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 2023 comprised loans for used passenger vehicles (50%) and big bikes (31%). The remaining 19% included loans for pickup trucks, vans, commercial trucks, and others.

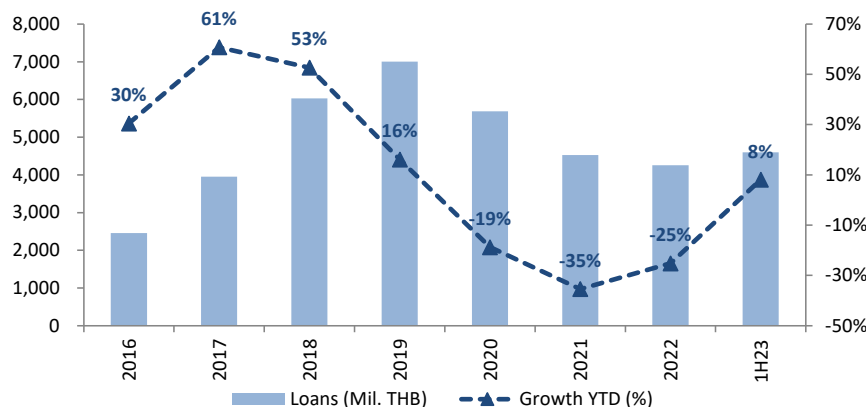
KEY OPERATING PERFORMANCE

Chart 1: ECL's Group Structure as of Sep 2023



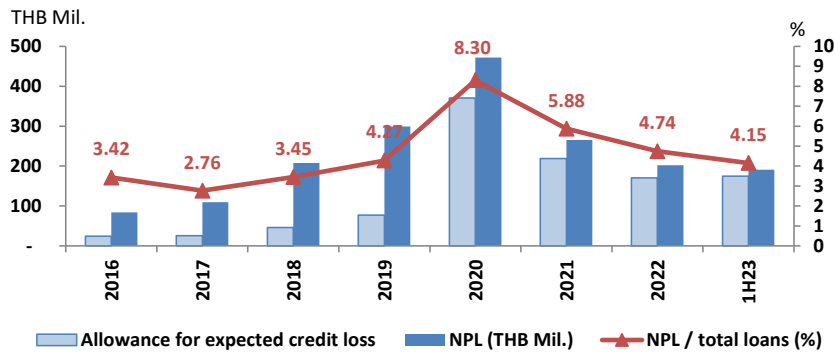
Source: ECL

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 2023	Year Ended 31 December			
	2022	2021	2020	2019	
Total assets	4,772	4,442	4,849	5,966	7,428
Total loans	4,599	4,255	4,523	5,687	7,002
Allowance for expected credit loss	175	170	219	371	77
Short-term debts	1,656	1,663	1,937	2,290	2,898
Long-term debts	1,131	838	1,018	1,862	2,539
Shareholders' equity	1,890	1,873	1,832	1,750	1,885
Net interest income	175	361	394	494	463
Expected credit loss	30	37	(23)	159	142
Non-interest income	86	161	161	191	232
Operating expenses	141	256	334	449	392
Earnings before taxes	90	229	244	77	160
Net income	72	185	194	62	130

* Consolidated financial statements

Unit: %

	Jan-Jun 2023	----- Year Ended 31 December -----			
		2022	2021	2020	2019
Profitability					
Net interest income/average assets	7.58 **	7.76	7.29	7.37	6.69
Non-interest income/average assets	3.75 **	3.46	2.98	2.85	3.35
Operating expenses/total income	44.57	41.03	48.40	49.85	42.54
Operating profit/average assets	3.89 **	4.93	4.51	1.15	2.32
Earnings before taxes/average risk-weighted assets	3.91 **	4.98	4.56	1.15	2.32
Return on average assets	3.12 **	3.97	3.59	0.92	1.88
Return on average equity	7.64 **	9.96	10.83	3.39	7.14
Asset Quality					
Receivable in stage 3/total loans	4.15	4.74	5.88	8.30	4.27
Expected credit loss/average loans	1.36 **	0.84	(0.44)	2.50	2.17
Allowance for expected credit loss/receivable in stage 3	91.49	84.37	82.37	78.52	25.79
Capitalization					
Risk-adjusted capital ratio	39.73	42.51	38.22	29.60	25.44
Debt/equity (times)	1.53	1.37	1.65	2.41	2.94
Funding and Liquidity					
Stable funding ratio	97.47	98.27	95.33	95.01	84.46
Liquidity coverage measure (times)	0.01	0.02	0.02	0.02	0.01
Short-term debts/total liabilities	59.42	64.74	64.20	54.31	52.29

** Annualized

RELATED CRITERIA

- Issue Rating Criteria, 15 June 2021
- Nonbank Financial Institution Methodology, 17 February 2020

Eastern Commercial Leasing PLC (ECL)

Company Rating:	BBB-
Rating Outlook:	Stable

TRIS Rating Co., Ltd.

Silom Complex Building, 24th Floor, 191 Silom Road, Bangkok 10500, Thailand Tel: +66 2 098 3000

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