TRIS RATING
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KRUNGTHAI CAR RENT & LEASE PLC

No. 195/2020
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FINANCIAL INSTITUTIONS

Company Rating:	A-
Outlook:	Stable

Last Review Date: 13/11/19

Company Rating History:

Date	Rating	Outlook/Alert
02/10/17	A-	Stable
15/05/08	BBB+	Stable

Contacts:

Preeyaporn Kosakarn

preeyaporn@trisrating.com

Siriwan Weeramethachai

siriwan@trisrating.com

Taweechok Jiamsakunthum

taweechok@trisrating.com

Narumol Charnchanavivat

narumol@trisrating.com

WWW.TRISRATING.COM

RATIONALE

TRIS Rating affirms the company rating on Krungthai Car Rent & Lease PLC (KCAR) at "A-" with a "stable" rating outlook. The rating reflects the company's stable market position in the operating lease business, low financial leverage, solid cash flow protection, and sufficient funding and liquidity. However, the rating is constrained by intense competition in the operating lease industry that continues to put pressure on the company's profitability.

KEY RATING CONSIDERATIONS

Sound business position maintained

TRIS Rating expects KCAR's market position as a mid-size operator to be maintained, supported by its brand equity, expertise in motor-vehicle operating lease, and comprehensive services. In 2019, the company ranked 7th among peers in terms of net leased assets with a share of 5.7%, compared with 5.0% (7th rank) in 2018 according to TRIS Rating's database.

The company has maintained its policies of avoiding competing on price and retaining prudent underwriting criteria to prevent deterioration in asset quality. We therefore expect its portfolio expansion to be gradual over the next few years. Despite adverse impacts stemming from the Coronavirus Disease 2019 (COVID-19) induced economic disruption, the company has managed to keep its portfolio value steady at THB4.2 billion as of September 2020, compared with THB4.3 billion at the end of September 2019.

Although the company specializes only in motor-vehicle operating lease, its busines position is supported by vertical integration within the business network of the Chantarasereekul family, the major shareholder and founder of the company. Such integration enables the company to operate more efficiently than its peers. It allows KCAR to purchase vehicles at relatively more favorable prices and sell retired vehicles with sound profit margins to retail customers via Krungthai Automobile Co., Ltd., the company's used-car dealer subsidiary.

Pressure on profitability from contract extension

The company's profitability has been under pressure, caused mainly by the extension of contract tenor to five years from three years. The shift has resulted in a decline in gross margin on operating lease due to lower average rental income received in each period, while maintenance costs have risen higher towards the end of contracts.

For the first nine months of 2020 (9M2020), gross margin on operating lease declined to 12.0%, from 15.5% in 9M2019. Gross margin on sales of retired vehicles also dropped to 27.4% in 9M2020, from 30.1% in 9M2019. As a result, overall profitability, measured by earnings before interest and tax (EBIT) margin, fell to 12.6% in 9M2020, from 13.0% in 9M2019.

The lower margin on sales of vehicles was caused largely by a larger proportion of vehicles being disposed through wholesale auctions where the margin tends to be lower than that of retail sales. However, this shift is viewed as an aberration caused by the disruption of retail sales during the COVID-19 pandemic.

We expect the EBIT margin to gradually improve over the long term. This is because the five-year contracts already accounted for 80% of all contracts, and we believe any additional pressure on operating lease margin should be manageable. With sales activity in the auto industry gradually normalizing, we expect the company to re-focus on disposing retired vehicles to retail customers through its auto dealership network. This should help sustain the gross margin on car sales at about 30% as seen in the past.

Leverage to remain relatively low

We believe the company's leverage level will likely remain relatively stable with debt to capitalization of around 50%-56% over the next few years, compared with 57.3% at the end of September 2020, the company should have less need for debt funding given its cautious approach to portfolio expansion. Also, the company's equity base is expected to be strengthened from lower dividend pay-out, to around 50% from 70%-80%. We also expect the company's debt to equity ratio (D/E) to remain below 2 times over the next few years, versus 1.6 times at the end of September 2020, and below the bond covenant of 3 times.

Strong cash flow protection

We expect the company's cash flow protection, as measured by the EBIT interest coverage ratio (EBIT/interest expenses), to remain healthy over the next few years despite a declining trend over past years resulting from margin compression. We project the company's EBIT interest coverage to be around 3-4 times in 2020-2023 as we believe the company will be able to sustain its EBIT level while maintaining its leverage and funding costs over the next few years. The company's funds from operations (FFO) to total debt ratio has also remained solid, with an annualized ratio of 40.1% for the first nine months of 2020.

Sufficient funding and strong liquidity profile

The company's funding and liquidity profile is supported by appropriate asset-liability management, relying on long-term borrowings as its main source of funds to match lease contract lengths of 3-5 years. At the end of September 2020, long-term borrowings made up 84% of the company's total borrowings. The company has financial flexibility thanks to its ability to access funding in both equity and debt capital markets. The company also had available credit facilities from various financial institutions totaling THB1.7 billion and THB500 million worth of hire-purchase credit facilities at the end of September 2020, which help serve as additional liquidity sources to cushion against any liquidity shortfalls.

BASE-CASE ASSUMPTIONS

TRIS Rating's base-case assumptions for KCAR in 2020-2023:

- Total lease portfolio to grow by 0%-5%.
- Operating lease gross margin to be around 12%.
- Cost of funds to hover around 3%.

RATING OUTLOOK

The "stable" outlook reflects our expectation that the company will maintain its market position and financial profile. The outlook is also based on our expectation that KCAR will maintain low financial leverage and sound cash flow protection, as well as sustain its financial performance.

RATING SENSITIVITIES

KCAR's credit upside would materialize if the company's market position improves significantly, leading to stronger financial performance and cash flow protection for a sustained period. On the contrary, the rating and/or outlook could be revised downward if the company's market position deteriorates significantly or if its financial performance or cash flow protection weakens with EBIT interest coverage falling below 2 times.

COMPANY OVERVIEW

KCAR was established in 1992 by Mr. Paitoon Chantarasereekul. The company was set up to provide corporate clients with long-term automobile rentals under operating lease contracts. The company also offers short-term auto rentals to both corporate and individual clients. From a base of THB4 million in 1992, the company's paid-up capital increased continuously as the business grew. In 2005, KCAR purchased a 95% stake in KA, a used car dealer, from the Chantarasereekul family. In 2012, KCAR acquired the remaining 5% stake in KA, which then became KCAR's wholly owned subsidiary.

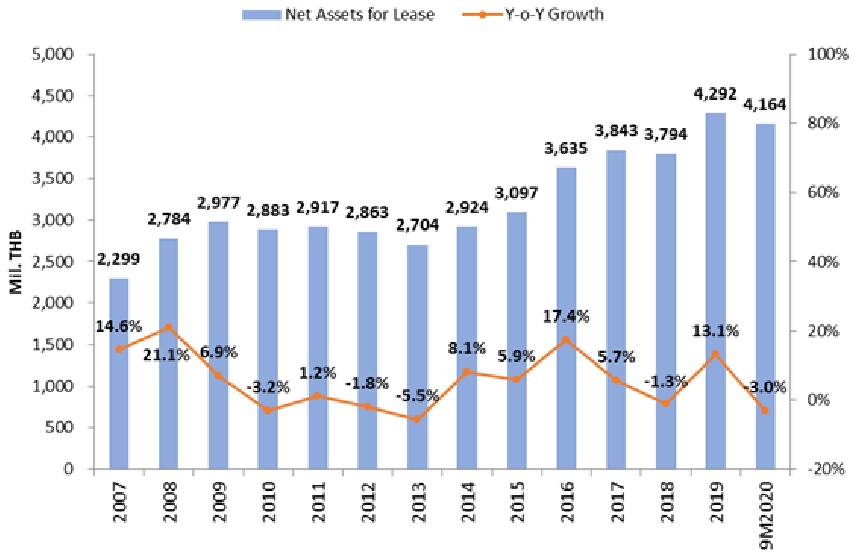
KCAR was listed on the Stock Exchange of Thailand (SET) in late 2005 and received THB212 million from the initial public offering (IPO). After the SET listing, the Chantarasereekul family has remained the major shareholder, controlling a majority stake of approximately 73.5% in KCAR as of March 2020.

KCAR provides rental services for various types of vehicles, including sedans, pick-up trucks, and vans. The company has a policy to concentrate on popular brands, especially Japanese cars, in order to reduce the risk of losses on retired assets. Preference is given to the "Toyota" brand, as the major shareholder owns a Toyota authorized dealership. KCAR also offers other brands, such as "Honda", "Isuzu", and "Nissan". In addition, the company rents some European brands to meet customer demand.

KCAR offers a full range of services, such as comprehensive insurance coverage, car registration, and vehicle maintenance. KCAR provides 24-hour customer service for both normal and emergency needs through a call center. The company also provides replacement cars in case of accident, loss, or lengthy repair.

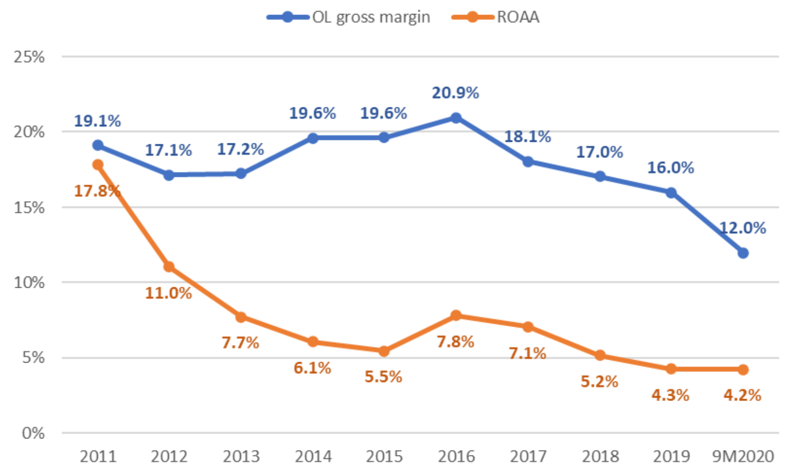
KEY OPERATING PERFORMANCE

Chart 1: KCAR's Net Assets for Lease



Source: KCAR

Chart 2: Operating Lease Gross margin and Return on Average Assets (ROAA)



Source: KCAR

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS

Unit: Mil. THB

	Jan-Sep 2020		2019	2018	2017	2016
			---------------Year Ended 31 December -----------			
Total operating revenues	1,653		1,967	2,081	2,091	2,002
Earnings before interest and taxes (EBIT)	209		259	296	395	404
Earnings before interest, taxes, depreciation, and amortization (EBITDA)	876		1,103	1,057	1,116	1,081
Funds from operations (FFO)	839		1,065	1,014	1,062	1,008
Adjusted interest expense	70		90	86	82	71
Capital expenditures	582		1,718	834	1,301	1,548
Total assets	5,308		5,531	4,833	4,999	4,640
Adjusted debt	2,787		3,061	2,386	2,614	2,337
Adjusted equity	2,078		2,055	2,027	2,014	1,982
Adjusted Ratios						
EBIT margin (%)	12.63		13.19	14.23	18.87	20.16
Return on average assets (%)	4.23	*	4.26	5.17	7.06	7.82
EBIT interest coverage (times)	2.99		2.87	3.44	4.83	5.69
FFO to debt (%)	40.08	*	34.78	42.51	40.62	43.12
Debt to capitalization (%)	57.28		59.83	54.07	56.48	54.10

* *Annualized with trailing 12 months*

RELATED CRITERIA

- Rating Methodology – Corporate, 26 July 2019

Krungthai Car Rent & Lease PLC (KCAR)

Company Rating:	A-
Rating Outlook:	Stable

TRIS Rating Co., Ltd.
Silom Complex Building, 24th Floor, 191 Silom Road, Bangkok 10500, Thailand Tel: 0-2098-3000