

THITIKORN PLC

No. 119/2020
31 July 2020

FINANCIAL INSTITUTIONS

Company Rating: A-
Outlook: Negative

Last Review Date: 24/07/19

Company Rating History:

Date	Rating	Outlook/Alert
31/03/10	A-	Stable
14/11/06	BBB+	Stable

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RATIONALE

TRIS Rating affirms the company rating on Thitikorn PLC (TK) at “A-” but revises the rating outlook to “negative” from “stable”. The change in outlook reflects a faltering market position in its core domestic business, motorcycle hire purchase. The rating continues to reflect the company’s solid capital base, resilient profitability, and healthy liquidity.

However, the key rating constraint is the potential decline in TK’s asset quality due to the relatively high credit risk of its customers who are susceptible to a weak economic environment. The rating also takes into account intense competition in the motorcycle hire purchase industry, particularly in the domestic market, which could limit margin improvement in the medium term. Significant increase in credit exposure in countries with higher country risk relative to Thailand could also negatively impact TK’s credit profile, if the credit risk is not well managed.

KEY RATING CONSIDERATIONS

Faltering domestic market position

TK’s domestic market position has gradually declined over the past few years. Its loan portfolio shrank by 18% year on year (y-o-y) to THB8.2 billion at the end of 2019. At the end of March 2020, outstanding loan contracted further to THB7.7 billion. This was mainly a result of its conservative growth strategy due to concerns over asset quality amidst the sluggish growth of the Thai and global economies. Although we view its cautious expansion strategy positively, the ongoing scale-down of business has significantly weakened its market position and customer base, both of which are factors underpinning its business position. This has led to our revision of the outlook to “negative”. Further weakening of these factors could put pressure on TK’s company rating. However, we expect the company’s new loans booking should have bottomed out in the first half of 2020 and that expansion mode will slowly resume starting from the second half of 2020 through 2021.

Geographically, the company has a well-diversified loan portfolio across Thailand as well as countries in the CLMV region, including Cambodia, the Lao People’s Democratic Republic (Lao PDR), and Myanmar. Nonetheless, we still expect the domestic portfolio to remain TK’s core business in the longer term.

Low leverage and strong capital base

TRIS Rating assesses TK’s capital position as very strong, with risk-adjusted capital (RAC) of 34.7% at the end of 2019. This capital position is stronger than its peers and appropriate for the relatively high credit risk profile of its target customers in the motorcycle hire purchase segment.

At the same time, TK’s financial leverage remains low as measured by the debt to equity (D/E) ratio of 0.72 times at the end of 2019, improving from 1.08 times at the end of 2018. The improvement in D/E ratio is due to a decline in debt obligations in line with the shrinkage of the loan portfolio and profit accretion in 2019. TRIS Rating expects TK’s capital to remain very strong in the medium term due to the slower pace of credit growth amid a weakening economy. Its robust capital provides a cushion to absorb credit cost that could potentially rise due to the economic fallout from Coronavirus Disease 2019 (COVID-19) pandemic.

Overseas expansion provides growth impetus

In the medium term, expansion in the overseas market will be a growth catalyst for TK, given its cautious growth strategy in the home market due to the fierce competition and a potential rise in credit risk. We expect overseas lending to constitute about 30%-40% of TK's total loan portfolio by 2023. This is based on the assumption that portfolio growth will continue at a similar pace to that in 2019. The company's total overseas exposure to its total portfolio increased to 18% at the end of 2019 from 10% at the end of 2018, of which 14% was from Cambodia and 4% from the Lao PDR. Overseas exposure increased further to 21% in the first quarter of 2020, mainly driven by Cambodia with a 17% contribution.

We also believe overseas operation will play increasingly vital roles in enhancing TK's profitability in the future as the overall return on overseas loans has been higher than the loans originated domestically. The positive aspects of operations in the CLMV region are the lower competition and the better asset quality relatively to the Thai market. That said, the non-performing loans (NPLs, loans more than 90 days past due) of the overseas subsidiaries began to increase in 2019. The total NPL ratio rose to 3% in 2019 from 1% in 2018. Although this is in line with our expectation given that loan portfolios have become more mature, further monitoring is required. For the geographic diversification to have a positive impact on TK's rating, it must help strengthen revenue while overall asset quality needs to be well maintained.

At the same time, the country risks of Cambodia, the Lao PDR, and Myanmar may need to be taken into consideration if these overseas loan portfolios contribute more significantly to TK's overall loan portfolio since these country risks are considered higher than that of Thailand.

Adequate liquidity

Liquidity is a positive rating factor for TK. We believe this is likely to remain so over the next few years due to the conservative expansion plan. As of March 2020 TK's cash on hand was THB941 million compared with pre-2018 where the average amount was around THB100-THB200 million.

The company relies more on long-term funding compared with its peers. However, due to the slowdown in TK's business, the need to refinance long-term borrowings has been low since 2019. The company's funding structure in 2019 comprised long-term borrowings (33.7%), short-term obligations (6.2%), and the current portion of long-term funding (60.1%).

As of March 2020, the company had a positive asset-liability duration gap. We expect TK to maintain a positive gap over the next 12 months. We estimate net cash inflows from customer loan repayments to amount to THB200-THB230 million per month over the next 12 months.

Sufficient provision for new accounting standard TFRS9

The company's asset quality is weak but comparable to peers in the same industry. The weak asset quality for the motorcycle hire purchase industry is caused in part by the high-risk credit profiles of the target customers, the majority of whom are from the underbanked group in the agricultural and manufacturing sectors. Moreover, the fierce competition in the industry has led to lax underwriting standards that focus on higher loan to value (LTV) to increase auto sale and loan approval while lowering repayment affordability for customers. Given the conservative growth strategy, TK has been able to maintain its NPL formation at between 9%-10% for the past four years. Despite the manageable asset quality over the past 4 four years, the NPL formation is considered high among the non-financial institutions. We expect TK's NPL formation to remain between 10%-11% given the current economic turmoil.

As of March 2020, the allowance for doubtful accounts stood at THB710 million. The reserves were in excess of the required amount based on its TFRS9 model, which resulted in a reversal of reserves by THB16 million. At the end of 2019, the ratio of allowance for doubtful accounts to NPLs (NPL coverage ratio) was at 194%. We estimate its credit cost to range between 10%-11% of total loans in 2020-2022.

BASE-CASE ASSUMPTIONS

TRIS Rating's base-case assumptions in 2020-2022 are:

- Outstanding portfolio to shrink in 2020 and to expand by 10%-15% per year in 2021-2022.
- RAC ratio to remain above 30%.
- Interest yield to remain above 31%-33%.
- Credit cost to remain at about 10%-11% annually.
- Operating expense to total income ratio will range from 50%-55%.

RATING OUTLOOK

The “negative” outlook reflects the consistently weakening market position of TK as observed from the steady contraction of motorcycle hire purchase business, the company’s core domestic business, which if continuing in the longer term could undermine TK’s business position.

RATING SENSITIVITIES

The rating outlook could be revised to “stable” if the market position in its core domestic business and revenues improve on a sustained basis. However, the rating could be downgraded if the company’s business position continues to weaken further or asset quality deteriorates to the extent that profitability declines significantly or leverage increases markedly as measured by a RAC ratio of less than 25%.

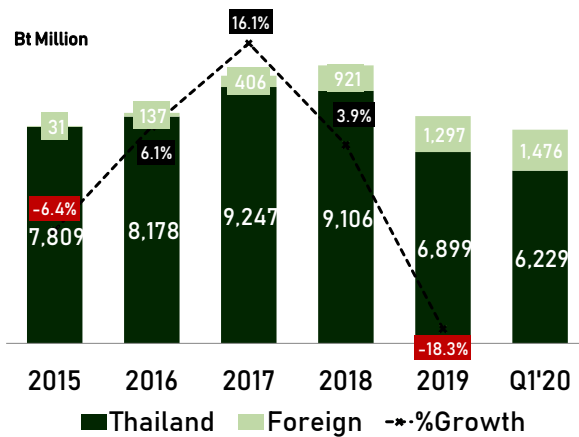
COMPANY OVERVIEW

TK was founded on 4 August 1972 by Dr. Chumpol and Dr. Anothai Phornprapha to provide motorcycle and automobile financing loans under hire purchase contracts. Currently, the company concentrates on the motorcycle financing segment. TK is more geographically diversified than its competitors. The company renders services through a branch network covering 56 provinces throughout Thailand. In addition, TK offers motorcycle loans in Cambodia and the Lao PDR through its subsidiaries, Suosdey Finance PLC and Sabaidee Leasing Co., Ltd., respectively, which were established in 2014.

As of March 2020, loans from TK comprised 77% of TK’s outstanding loans; 17% from Suosdey (Cambodia based subsidiary) and 4% from Sabaidee (Laos based subsidiary) and another 2% from other subsidiaries.

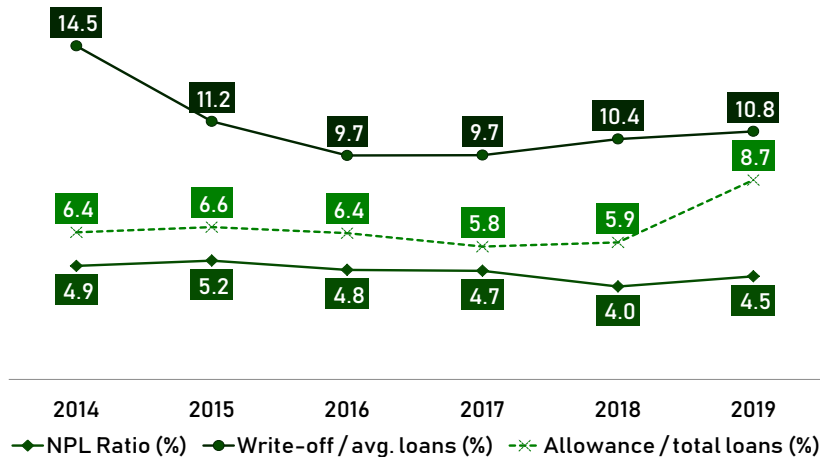
KEY OPERATING PERFORMANCE

Chart 1: Outstanding Loans



Source: TK

Chart 2: Asset Quality



Source: TK

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS*
Unit: Mil. THB

	Jan-Mar 2020	----- Year Ended 31 December -----			
		2019	2018	2017	2016
Total assets	8,482	9,163	10,578	10,018	8,611
Total loans	7,705	8,195	10,027	9,653	8,315
Allowance for doubtful accounts	882	710	597	557	528
Short-term borrowings	1,999	2,251	2,436	976	1,481
Long-term borrowings	632	1,145	2,569	3,812	2,204
Shareholders' equity	5,430	5,324	5,078	4,785	4,550
Net interest income	581	2,858	3,063	2,802	2,442
Bad debts and doubtful accounts	192	1,094	1,067	903	795
Non-interest income	136	730	670	729	789
Operating expenses	397	1,862	2,154	2,024	1,902
Net income	103	510	402	472	430

* Consolidated financial statements

Unit: %

	Jan-Mar 2020	----- Year Ended 31 December -----			
		2019	2018	2017	2016
Profitability					
Net-interest income/average assets	26.32 **	28.96	29.74	30.08	28.90
Net-interest income/total income	78.38	79.96	79.30	76.91	72.86
Operating expenses/total income	53.58	50.13	55.78	55.55	56.74
Operating profit/average assets	5.78 **	6.41	4.97	6.49	6.33
Earnings before taxes/average risk-weighted assets	3.47 **	3.67	2.72	3.55	3.54
Return on average assets	4.68 **	5.16	3.90	5.07	5.09
Return on average equity	7.68 **	9.80	8.14	10.12	9.70
Asset Quality					
Non-performing loans/total loans	7.12	4.47	4.03	4.71	4.76
Bad debts and doubtful accounts/average loans	9.65 **	12.01	10.84	10.05	9.84
Allowance for doubtful accounts/total loans	11.44	8.66	5.95	5.77	6.35
Capitalization					
Risk-adjusted capital ratio	38.51	34.70	26.46	26.01	29.07
Shareholders' equity/total loans	70.47	64.96	50.64	49.57	54.72
Debt to equity (time)	0.56	0.72	1.08	1.09	0.89
Liquidity					
Stable funding ratio	78.67	78.93	76.27	89.07	81.22
Liquidity coverage measure (times)	2.10	3.90	3.22	6.92	4.32
Short-term borrowings/total liabilities	65.48	58.62	44.29	18.64	36.46
Total loans/total assets	90.84	89.44	94.79	96.35	96.56

* Consolidated financial statements

** Annualized

RELATED CRITERIA

- Nonbank Financial Institution Methodology, 17 February 2020

Thitikorn PLC (TK)

Company Rating:

A-

Rating Outlook:

Negative

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