

GROUP LEASE PLC

No. 174/2018
2 November 2018

FINANCIAL INSTITUTIONS

Issue Rating:

Partially guaranteed BB+

Outlook: Negative

Last Review Date :

Date	Rating	Outlook/Alert
25/04/18	BB+	Alert Negative

Issue Rating History:

Date	Rating	Outlook/Alert
18/10/17	BB+	Alert Negative
05/04/17	A-	Negative
05/02/14	A-	Stable

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RATIONALE

TRIS Rating affirms the rating on the outstanding partially guaranteed debentures of Group Lease PLC (GL) at “BB+”. At the same time, TRIS Rating replaces the “negative” CreditAlert on the outstanding senior partially guaranteed debentures with a “negative” outlook. The revised outlook reflects concerns over GL’s weaker business and financial profile and uncertainty stemming from open litigation issues.

The rating on the partially guaranteed debentures is based on the credit profiles of both the guarantor and the issuer (GL). Sixty-five percent (65%) of the sum of the outstanding principal plus interest is guaranteed by KASIKORNBANK PLC (KBANK), rated “BBB+” by S&P Global Ratings, with a “stable” outlook (international scale). The guarantee given by KBANK is unconditional and irrevocable.

On the issuer side, GL’s credit profile has been weak since 2017, due to deterioration in financial profile and concentration of its operating assets in higher-risk countries than Thailand. However, GL’s capitalization is adequate to absorb some risks, a fact which mitigates some of the concerns underlying the rating.

KEY RATING CONSIDERATIONS

Weak credit profile after suspending interest payments on CDs

As of June 2018, GL’s funding totaled were Bt13,996 million, broken down as equity (42.1%), convertible debentures (CDs) (46.9%), the partially guaranteed debentures (10.6%), and other sources (0.4%).

J Trust Asia Pte. Ltd. (JTA) is GL’s opponent in several lawsuits. JTA owns CDs issued by GL equivalent to Bt5,922 million worth of 90.1% of the entire amount outstanding. On 9 January 2018, JTA filed civil lawsuits against GL and its subsidiary, nullifying the transaction of those convertible debentures. JTA demanded GL repay approximately Bt6,000 million for the CDs and pay an additional Bt2,000 million in damages. The court dismissed the case since 19 March 2018, and now the case is under the appeal process requested by JTA.

GL suspended interest payments on the CDs issued to JTA, based on the legal opinion from GL’s external counsel. The interest miss payments have weakened GL’s credit profile. The value of the interest mispayment amounts to Bt329.32 million. GL has accrued such withheld interest in the financial statement for the first quarter 2018. In addition, the company continues to service its other debt obligations as scheduled.

Uncertain outcome from litigation may impact liquidity

At the end of June 2018, GL held a large amount of cash and cash equivalents, amounting to Bt3,266 million (22.2% of total assets). The ample cash balance, plus the monthly loan payments from GL’s customers, lessens the liquidity concerns surrounding the Bt1,500 million partially guaranteed debenture maturing in September 2019. GL believes that the timeline of the litigation process will be longer than the maturity of the partially guaranteed debentures.

However, uncertain result of the litigation could have a significant effect on GL. For example, if JTA wins and GL has to pay the entire amount demanded, GL could face a short-term liquidity shortage. In particular, some portion of assets

are pledged for backing up the partially guarantee debentures, which might limit GL's financial flexibility to access new funding.

Extra allowances affect financial performance

GL's financial performance declined considerably in 2017. GL reported a net loss of Bt1,607 million for the year 2017. The loss was due primarily to two factors. GL made allowances for the small and medium enterprise (SME) loans (which were made to two groups of borrowers, including companies registered in Cyprus and in Singapore). GL also set aside an allowance in the third quarter to a loss in an associated company.

For the first half of 2018, normal operations declined. The annualized return on average assets (ROAA) dropped to 3.2%, from 6.1% during the same period in 2017. Operating expenses rose, as did bad debt expense. The ratio of provision expenses to average loans rose to 5.3% for the first half of 2018, up from 4.5% in 2017. The ratio of losses on repossessed motorcycles to average loans decreased slightly to 3.39% in 2017, from 3.47% in 2016.

49% of assets concentrated in higher risk countries than Thailand

GL began to diversify its business overseas in 2013. Assets and investments abroad comprised around 49% of total assets at the end of 2017. The investments were made in nearby countries, such as Cambodia (22% of total assets), Sri Lanka (14%), Laos (5.4%), Myanmar (4.2%) and Indonesia (3.2%). However, these countries have higher country risk than Thailand, and business operation in these countries has been considered as a short track record to prove a stable success, which might expose GL to uncertain operating environment and consequently lead GL to business volatility and uncertain downside risks in the future.

Deteriorated asset quality and impairment risk in investment

The quality of GL's loan portfolio has deteriorated. The ratio of non-performing loans (NPLs; loans overdue more than three months) to total loans rose to 5.0% at the end of June 2018, from 4.3% at the end of 2017. The NPL ratio increased because asset quality deteriorated in Thailand and abroad. TRIS Rating expects GL will strengthen its underwriting and collection systems. As a result, the quality of the loan portfolio will remain acceptable.

In addition, GL expanded to Sri Lanka in December 2016 through Group Lease Holdings Pte. (GLH), a wholly-owned subsidiary registered in Singapore as a holding company, by way of a Bt2,489 million equity investment in Commercial Credit and Finance PLC (CCF). GL's investment gave it 29.99% of the share capital of CCF. The investment in Sri Lanka may bring new growth opportunities, but GL will also face asset impairment risk. Using the equity method, GL's balance sheet showed the value of the investment in CCF at Bt2,085 million at the end of June 2018, a 16.2% drop from the initial investment value.

Adequate capitalization

GL's capital base will serve two main purposes: give it a base from which to expand abroad, and serve as a cushion to protect against losses, given the risky nature of its target customers. The ratio of shareholders' equity to total assets declined to 39.8% at the end of 2017, from 48.5% at the end of 2016. Extra loan loss allowances caused a net loss in 2017. At the end of June 2018, the ratio remained steady at 40%. Despite the recent slide, the capital base is adequate to support the high-risk nature of the motorcycle financing business and to finance a normal expansion of the loan portfolio.

According to a key financial covenant for the outstanding debentures, the debt to equity ratio must stay below ~~five~~ 5.0 times. The debt to equity ratio at the end of June 2018 was 1.5 times. Thus, the company was in compliance. TRIS Rating believes that the company will easily stay in compliance for the next 12 months.

RATING OUTLOOK

The "Negative" outlook for GL's issue rating reflects its weak credit profile, the result of the uncertainty surrounding the pending litigation.

RATING SENSITIVITIES

The downside case for the issue rating would emerge if any new uncertainties arise, if asset quality or profitability deteriorates further than TRIS Rating's expectation, or if the creditworthiness of KBANK, the guarantor, weakens. The upside case hinges in the credit profile of the guarantor or the issuer.

COMPANY OVERVIEW

GL was founded in 1986 by the Luaengrunsi family to make automobile hire purchase loans. In 1990, the company was acquired by Mr. Khanchai Boonpan and Mr. Anusak Intharaphuvasak. The company then shifted to focus on hire purchase

loans for motorcycles. The company's market position improved in 2005 after listing on the Stock Exchange of Thailand (SET) in 2004. In 2007, The Asia Partnership Fund (APF) conglomerate acquired all the shares held by the major shareholders and made a tender offer to the remaining retail shareholders. APF has been GL's major shareholder since then. As of June 2018, APF's shareholding in GL comprised Engine Holdings Asia Pte., Ltd. (26.4% stake), A.P.F. Holdings Co., Ltd. (10.4%), and Six Sis Ltd. (12.2%).

In 2013, GL started offering hire purchase loans in Cambodia through its wholly-owned subsidiary, GL Finance PLC (GLF). The company cooperates with Honda NCX, the sole authorized manufacturer and distributor of Honda motorcycles in Cambodia. Currently, GLF's portfolio comprises hire purchase loans for motorcycles, Kubota farm equipment, and solar panels.

In 2014, GL started providing loans in the Lao PDR through a subsidiary, GL Leasing (Lao) Co., Ltd. (GLL). GLL uses a business model similar to the approach GLF takes in Cambodia. GLL focuses on loans for agricultural machinery and motorcycles.

In July 2014, GL acquired all the shares of Thanaban Co., Ltd. (TNB) from Thai Credit Retail Bank PLC (TCRB). TNB is a well-known, medium-sized motorcycle financing firm. TNB's loan portfolio held around Bt1,500 million in outstanding loans during 2013 and 2014. The acquisition of TNB helped GL improve its market position in terms of outstanding loans. In addition, GL benefits from TNB's dealership network.

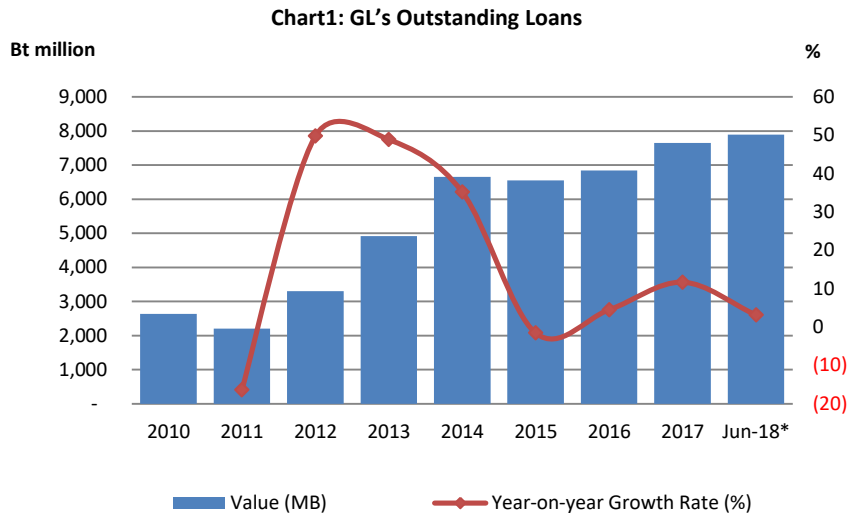
GL also expanded to Indonesia through a subsidiary, PT Group Lease Finance Indonesia (GLFI), a joint venture between Group Lease Holdings Pte., Ltd. (GLH), J Trust Asia Pte., Ltd., and a local Indonesian company. GLFI received an official license from the Indonesian authorities (OJK) in July 2016.

GL expanded to Sri Lanka in December 2016 through GLH, by way of a Bt2,489 million equity investment in CCF. An asset impairment charge of Bt583 million has cut the value of the investment. Using the equity method, GL's balance sheet reflected the value of the investment in CCF at Bt2,545 million at the end of 2016, Bt2,023 million at the end of 2017, and at Bt2,085 million at the end of June 2018.

As of June 2017, GL's assets were Bt18,277 million. SME loans provided to two groups of borrowers (companies registered in Cyprus and in Singapore) made up almost one-fifth or approximately 17% of assets. In October 2017, the Securities and Exchange Commission (SEC) alleged and later concluded that almost 60% of the SME loans, or also known as the Disputed Loans, were fraudulent. The company then set aside provisions for the entire outstanding amount of the loans, in response to an SEC order to revise and correct past financial statements. The provisions were reflected in the financial statements ending 30 September 2017.

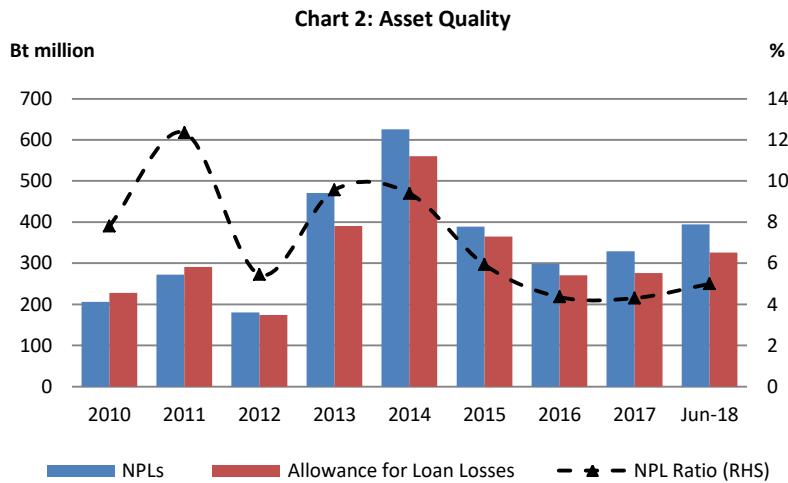
At the end of June 2018, the largest portion, or 51.4% of assets, comprised four types of loans: hire purchase loans, asset-backed loans, microfinance loans, and consumer finance loans made to borrowers in Thailand, Cambodia, the Lao People's Democratic Republic (Lao PDR), Myanmar, and Indonesia. Cash and cash equivalents amounted to 22.2% of assets. The remainder was the investment in CCF in Sri Lanka (14.2%), investments in other companies in Singapore, Indonesia, and Myanmar (4.6%), and other assets (7.6%).

KEY OPERATING PERFORMANCE



Source: GL

* Year-to-date growth for Jun-18



Source: GL

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS*

Unit: Bt million

	Jan-Jun 2018	----- Year Ended 31 December -----			
		2017	2016	2015	2014
Total assets	14,713	14,382	17,029	10,765	7,272
Total loans**	7,891	7,650	6,849	6,553	6,656
Adjusted loans***	9,485	9,219	10,370	9,311	6,719
Allowance for doubtful accounts	326	276	271	365	560
Short-term borrowings	98	191	1,646	1,911	2,818
Long-term borrowings	8,059	7,963	6,172	998	1,800
Shareholders' equity	5,897	5,726	8,264	7,581	2,514
Net interest income	1,042	2,090	2,045	1,831	1,431
Bad debts and doubtful accounts	206	323	313	357	495
Expenses Allowance on SME loans	-	1,560	-	-	-
Non-interest income	267	614	419	391	181
Operating expenses	806	3,837	1,120	1,139	979
Net income	233	(1,607)	829	583	118

Unit: %

	Jan-Jun 2018	----- Year Ended 31 December -----			
		2017	2016	2015	2014
Profitability					
Net-interest income/average assets****	14.33	13.31	14.72	20.30	22.41
Net-interest income/total income	69.23	66.36	74.72	73.55	76.84
Operating expenses/total income	53.57	44.16	40.91	45.78	52.59
Operating profit/average assets****	4.07	(9.26)	7.42	8.05	2.16
Return on average assets****	3.20	(10.23)	5.97	6.46	1.84
Return on average equity****	8.00	(22.97)	10.46	11.55	4.93
Asset Quality					
Non-performing loans/total loans**	5.00	4.31	4.36	5.93	9.40
SME non-performing loans/adjusted loans***	16.80	17.02	-	-	-
Bad debts and doubtful accounts/average total loans**,****	5.31	4.46	4.68	5.40	8.55
Expenses allowance on SME loans/average adjusted loans***,****	-	16.02	-	-	-
Allowance for doubtful accounts/total loans**	4.13	3.61	3.96	5.56	8.42
Allowance for doubtful accounts/non-performing loans	82.68	83.78	90.75	93.78	89.61
Capitalization					
Shareholders' equity/total assets	40.08	39.81	48.53	70.43	34.57
Shareholders' equity/total loans**	74.32	74.84	120.67	115.69	37.77
Debt to equity (times)	1.49	1.51	1.06	0.42	1.89
Liquidity					
Short-term borrowings/total liabilities	1.12	2.21	18.77	60.03	59.21
Total loans**/total assets	53.93	53.48	60.90	86.49	92.39

* Consolidated financial statements

** Total loans include hire purchase loans, asset-backed loans, microfinance loans, and consumer finance loans.

*** Adjusted loans include hire purchase loans, asset-backed loans, microfinance loans, consumer finance loans, and SME loans.

**** Annualized

RELATED CRITERIA

- Nonbank Lending Company, 7 May 2018

Group Lease PLC (GL)

Issue Rating:

GL199A: Bt1,500 million partially guaranteed debentures due 2019

BB+

Rating Outlook:Negative

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