TRIS RATING
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AAPICO HITECH PLC

No. 113/2023
23 June 2023

CORPORATES

Company Rating: A-
Outlook: Stable

Last Review Date: 30/06/22

Company Rating History:

Date	Rating	Outlook/Alert
30/06/21	BBB+	Stable
07/07/20	BBB+	Negative
22/07/19	BBB+	Stable
24/08/18	BBB+	Positive
12/11/14	BBB+	Stable

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RATIONALE

TRIS Rating upgrades the company rating on AAPICO Hitech PLC (AH) to "A-" from "BBB+", with a "stable" outlook. The rating upgrade is based on our expectation that the company will consistently deliver strong operating performance while maintaining financial metrics at our target levels. The rating also reflects AH's strong competitive position as a Tier-1 automotive parts manufacturer in Thailand. However, these strengths are somewhat offset by the company's customer concentration risk, challenges associated with overseas operations and an ongoing legal dispute, as well as the cyclical nature of the automotive industry.

KEY RATING CONSIDERATIONS

Consistently strong performance anticipated

AH recently reported record high revenue and earnings, supported by the robust performance of its original equipment manufacturer (OEM) auto parts and car dealership businesses. We expect this momentum to continue over the next 2-3 years, driven by increasing orders from both new and existing clients in the OEM auto parts business, as well as continued expansion of showrooms for the car dealership business.

In 2022, AH's total operating revenue surged to THB28.3 billion, marking a 36.3% year-on-year (y-o-y) increase. Additionally, its earnings before interest, taxes, depreciation, and amortization (EBITDA) rose significantly to THB3.2 billion, representing a 51.9% y-o-y growth. This positive momentum carried into the first quarter of 2023, despite a slowdown in the global economy. In our view, continued solid orders from customers should ensure satisfactory performance for AH in the next couple of years.

Under our base-case forecast, we project AH's total operating revenue to range from THB29-THB30 billion per annum during 2023-2025. The company's EBITDA is expected to stay in the range of THB2.7-THB3.2 billon per annum, with an EBITDA margin of 9%-11%. Although the profit margin is rather low, the company's ability to pass through increases in raw material costs to automakers and efficient production management should help maintain the margin within the target range.

Declining financial leverage

The improved operating performance recently enhanced AH's cash flow protection. Its debt to EBITDA ratio declined significantly to 1.9 times in the first quarter of 2023, from a peak of 5.3 times in 2020. Furthermore, its funds from operations (FFO) to debt ratio rose to 45.5% in the first quarter of 2023, compared with 14.3% in 2020.

Looking ahead, we believe AH will maintain its financial metrics as targeted. That is, the debt to EBITDA ratio should remain below 2.5 times and the FFO to debt ratio should stay above 30%. Under our base-case scenario, AH's annual FFO of THB2.2-THB2.7 billion should be sufficient to support annual capital expenditures and investments of THB1-THB2 billion over the next three years. Dividend payments are set at approximately 30% of net profit. Therefore, we expect AH's capital structure to remain strong, with a debt to capitalization ratio of about 40% over the next three years.

A financial covenant on its debentures requires AH to maintain the net total liabilities to equity ratio below 2 times. As of March 2023, the ratio stood at

1.4 times. TRIS Rating believes that AH will remain compliant with the covenant for the next 12 to 18 months. As for the debt structure, at the end of March 2023, AH's consolidated debt (excluding lease obligations) amounted to THB7.1 billion, of which THB3.3 billion was priority debt, comprising secured debt owed by AH and all borrowings incurred by its operating subsidiaries. The priority debt to total debt ratio was 46%.

Competitive strength in automotive parts business

We believe AH will maintain its strong position in the OEM auto parts business, considering its long market presence, close relationships with customers, and large-scale business. With almost 30 years of experience, the company has supplied auto parts for major automakers and Tier-1 parts makers such as Isuzu, Ford, Mazda, Nissan, DANA, and Continental. The reliability of AH's operations and its credibility have helped establish strong relationships with these customers.

Additionally, AH's business scale is relatively large. Revenue from the OEM auto parts business nearly doubled to THB20.3 billion in 2022, from THB10.6 billion in 2018. The large business scale benefits the company in terms of the ability to handle large orders from numerous customers, creating a barrier to entry. Moreover, AH's ability to control costs and deliver quality products on time helps boost orders from both existing and new customers.

Customer concentration risk

AH is the sole pickup chassis frame supplier for Isuzu and Mazda BT-50 in Thailand. Sales to Isuzu accounted for 20%-30% of AH's total revenue while sales to Ford and Auto Alliance (AAT; a Ford and Mazda joint venture) made up 7%-8% during the past three years. Isuzu and AAT are among the top five largest automakers in Thailand based on total car production volume. AH's longstanding relationships with and continued orders it has received from these customers partly help mitigate concerns over the concentration. Generally, automakers and Tier-1 parts makers are reluctant to change their major suppliers due to high switching costs and concerns over product quality.

Looking ahead, we anticipate AH will benefit from the relocation of several Chinese automakers to Southeast Asian countries amid concerns over geopolitical tensions. The increasing demand for electric vehicles and the strong automotive supply chain in Thailand are also expected to attract Chinese automakers. Apart from the customer base expansion, AH's overseas diversification also helps mitigate concentration risk. Nonetheless, the EBITDA contribution from its overseas investments remained below one fourth of the total in 2022.

Overseas diversification poses both opportunities and challenges

As a main part of its growth strategy, AH has expanded internationally, investing nearly THB7 billion in Sakthi Global Auto Holdings Ltd. (SGAH), a producer of steering knuckles, through equity and loan financing. AH expected the investment to help enhance its business scale and establish a footprint in the global market since SGAH had production bases in several countries, including India, Portugal, China, and the United States (US). However, SGAH underperformed, failing to repay its loans to AH. As a result, AH exercised its rights to appropriate the remaining shares of SGAH, pledged as collateral, and impaired its investment, amounting to about THB1.1 billion in 2019. In addition, AH purchased a 100% stake in Sakthi Portugal S.A., owned indirectly by SGAH, from a secured lender in order to obtain full management control. Sakthi Portugal S.A. was later renamed AAPICO Maia S.A. (MAIA).

Currently, AH directly owns 100% shares in SGAH and MAIA. SGAH owns about 77% of Sakthi Auto Component Ltd. (SACL) in India. The operating performance of MAIA, based in Portugal, has gradually recovered after the easing of Coronavirus Disease 2019 (COVID-19) controls and chip shortages. Our forecast expects the Portuguese operation to continue generating approximately THB4 billion in annual revenue and THB0.4 billion in annual EBITDA for AH over the next three years.

Meanwhile, the Indian operation is still embroiled in a legal dispute with the previous shareholders of SGAH. Despite owning a 77% stake in SACL, AH has no control over it. AH's attempt to resolve the issue is still ongoing. Due to limited access to financial information of the Indian operation, the auditor has given a qualified opinion on AH's financial statements. AH realized THB159 million in shared profits, without dividends, from the Indian operation in 2022. Thus, AH's EBITDA, based on our calculation, did not include the operating performance of SACL. The investment in the Indian operation totaled THB2.7 billion, making up about 10% of AH's total assets as of March 2023. In our base case, we do not expect any further material adverse impacts on AH from the ongoing dispute.

Manageable liquidity

We assess AH's liquidity as manageable. At the end of March 2023, AH had approximately THB3.7 billion in debt coming due in the next 12 months, comprising THB1.9 billion in short-term loans for working capital, THB1.5 billion in long-term bank loans, and THB0.3 billion in debentures. AH's cash and marketable securities totaled nearly THB1 billion. FFO over the next 12 months is forecast to be THB2.4 billion. Additionally, AH had undrawn uncommitted credit facilities worth approximately THB4 billion.

BASE-CASE ASSUMPTIONS

Key assumptions in TRIS Rating's base-case forecast during 2023-2025 are as follows:

- Total operating revenue to be THB29-THB30 billion per annum.
- EBITDA margin to range from 9%-11%.
- Capital expenditures and investments to stay in the THB1-THB2 billion per annum range.

RATING OUTLOOK

The "stable" outlook reflects our expectation that AH will maintain its competitiveness in its core lines of business. The company is expected to maintain satisfactory operating performance with well-managed leverage. The ability to pass through increases in raw material prices should help AH handle rising cost pressure. In addition, the ongoing legal dispute is not anticipated to have any material adverse impacts on AH.

RATING SENSITIVITIES

The rating upside is limited in the near term. However, it could happen if AH can significantly enhance its earnings bases and leverage stays under control. In contrast, the rating and/or outlook could be downgraded if the company's operating performance falls significantly below estimates, resulting in its EBITDA staying below THB2.5 billion per annum and/or the debt to EBITDA ratio rising above 3 times for an extended period.

COMPANY OVERVIEW

Established in 1996, AH is a large Tier-1 manufacturer of automotive parts in Thailand. The company started as a Ford distributor, before expanding to the manufacture of auto parts. It was listed on the Stock Exchange of Thailand (SET) in 2002. As of March 2023, the major shareholder of AH remained the Yeap family, holding about 39% of the outstanding shares.

AH has two core lines of business: OEM auto parts and car dealerships. The company's OEM products are stamped or pressed parts, forged, cast and machined parts, plastic parts, and jigs and dies. The key OEM products are stamped or pressed parts including chassis frames. The car dealership business sells Ford, Mitsubishi, MG, and Mazda vehicles in Thailand and Honda and Proton vehicles in Malaysia. AH also imports and distributes several brands of motorcycles comprising Bajaj, KTM, and Husqvarna.

The OEM auto parts business accounts for 70%-80% of its total revenue annually, while the car dealership business constitutes the rest. In the first quarter of 2023, AH's operations in Thailand contributed 67% of total revenue, followed by operations in Portugal (15%), Malaysia (14%), and China (4%).

KEY OPERATING PERFORMANCE

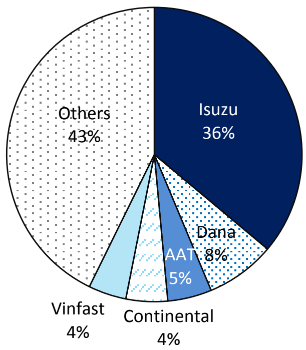
Table 1: Revenue Breakdown

Unit: %

Sources of Revenue	2019	2020	2021	2022	Jan-Mar 2023
OEM auto parts	70	70	74	73	73
Car dealership	30	30	26	27	27
Total	**100**	**100**	**100**	**100**	**100**
Total revenue (mil. THB)	**18,389**	**17,419**	**20,433**	**27,967**	**8,126**

Source: AH

Chart 1: Major OEM Customers in 1Q23



Source: AH

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS*

Unit: Mil. THB

	Jan-Mar 2023	2022	2021	2020	2019
		-------------Year Ended 31 December ------------			
Total operating revenues	8,197	28,285	20,746	17,798	18,959
Earnings before interest and taxes (EBIT)	765	2,307	1,279	565	1,493
Earnings before interest, taxes, depreciation, and amortization (EBITDA)	1,085	3,247	2,138	1,757	2,923
Funds from operations (FFO)	920	2,741	1,696	1,340	2,383
Adjusted interest expense	91	346	350	376	312
Capital expenditures	317	1,005	1,469	638	1,003
Total assets	25,754	25,469	22,722	22,346	21,293
Adjusted debt	6,710	7,288	7,726	9,351	8,580
Adjusted equity	10,521	9,929	8,815	7,741	7,481
Adjusted Ratios					
EBITDA margin (%)	13.24	11.48	10.30	9.87	15.42
Pretax return on permanent capital (%)	14.34 **	13.06	7.29	3.28	9.55
EBITDA interest coverage (times)	11.89	9.39	6.11	4.67	9.36
Debt to EBITDA (times)	1.85 **	2.24	3.61	5.32	2.94
FFO to debt (%)	45.55 **	37.61	21.96	14.33	27.78
Debt to capitalization (%)	38.94	42.33	46.71	54.71	53.42

* *Consolidated financial statements*
** *Adjusted with trailing 12 months*

RELATED CRITERIA

- Corporate Rating Methodology, 15 July 2022
- Key Financial Ratios and Adjustments for Corporate Issuers, 11 January 2022
- Issue Rating Criteria, 15 June 2021

AAPICO Hitech PLC (AH)

Company Rating:	A-
Rating Outlook:	Stable

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