

Ayudhya Development Leasing Company Limited

Company Rating:

BBB+

Rating Outlook:

Stable

Rating Rationale

TRIS Rating assigns the company rating of Ayudhya Development Leasing Co., Ltd. (ADLC) at “BBB+”. The rating reflects ADLC’s strong market position in the industrial machinery and equipment leasing industry, an experienced management team, and the company’s low operating costs compared with peers, as well as business and financial support from its major shareholder, Bank of Ayudhya PLC (BAY). However, these strengths are partially offset by customer concentration risk and the relatively weak credit profiles of its target customers compared with customers of commercial banks.

ADLC is a leading financial leasing company that concentrates on industrial machinery and equipment leases. The company was established in 1991 as a joint venture of three financial institutions: BAY, International Finance Corporation (IFC) and Korea Development Leasing Corporation (KDLC) -- the largest leasing company in South Korea. BAY Group’s ownership in ADLC increased from initially 40% to currently 76%. As part of the BAY Group, ADLC supports BAY’s strategy to be a universal banking. Therefore, TRIS Rating expects that BAY will continue to provide business cooperation and financial support to ADLC.

Fourteen years of operation, together with the support of its foreign partners and the extensive experience of its management team, help ADLC to continuously expand its loan portfolio. The company has a proven record of prudently managing its operating costs. During 2000-2003, its ratio of operating expenses to total income was approximately 14.5% compared with 27.8% for its peers.

ADLC’s small customer base of around 200 clients exposes the company to customer concentration risk. Most of its customers are small- and medium-sized entities, who may have difficulty obtaining loans from commercial banks because of a lack of strong audited financial statements. The characteristics of the leasing business and ADLC’s policies, such as requiring deposits for lease rental, securing buy-back guarantees from suppliers, and assigning payments from lessees’ customers, will mitigate potential losses from defaulting accounts to some extent. However, the long period required for the disposition of lease assets and the higher probability of default from customers with sub-prime credit compared with the customer bases of commercial banks may lead to burden some loss provisions and hamper future profitability of ADLC.

Rating Outlook

The “stable” outlook reflects TRIS Rating’s expectation that ADLC’s experienced management team will be able to expand its portfolio, continuously generate sufficient yields, and maintain low operating costs. The rating is based on the assumption that BAY will continue to provide both business and financial support to ADLC.

Key Rating Considerations

Strengths/Opportunities

- One of the market leaders in industrial machinery and equipment leasing
- Support from BAY
- Adequate capitalization

Weaknesses/Threats

- Sub-prime customer credit profiles
- Customer concentration risk

Corporate Overview

Ayudhya Development Leasing Co., Ltd. (ADLC) was established in 1991 through collaboration between Bank of Ayudhya PLC (BAY), International Finance Corporation (IFC) and Korea Development Leasing Corporation (KDLC) to enter into the leasing business. ADLC is one of the leading industrial machinery and equipment leasing operators in Thailand. The company provides financial leases to various industries, such as manufacturing, construction, transportation and healthcare. For the first six years of operation, ADLC’s overall portfolio continuously increased, from Bt65 million at the end of 1992 to a peak of Bt3,469 million at the end of 1997. The impact from the 1997 financial crisis was widespread and ADLC suffered from foreign-denominated debt, mismatched assets and liabilities, and deteriorating asset quality. However, support from its shareholders enabled ADLC to refinance short-term loans with long-term loans and this, along with a new capital injection, strengthened ADLC’s capital base, enabling the company to move ahead.

loans fell from 43% at the end of 1999 to 30% at the end of 2004 while the proportion of transportation equipment loans rose from 10% to 28% over the same time period. The number of lessees increased from 125 clients at the end of 2000 to 206 clients at the end of 2004. At the same time, the number of executed contracts doubled from 267 contracts at the end of 2000 to 540 contracts at the end of 2004, while the average contract size slightly decreased from Bt7.5 million to Bt6.8 million over the same period.

Recent Developments

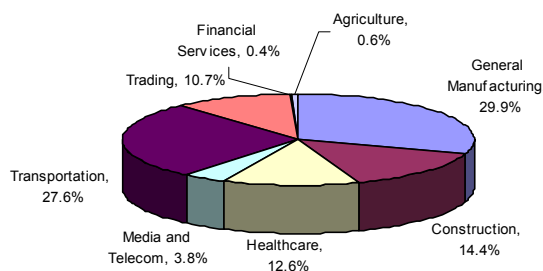
▪ **Capital injection from BAY**

Underwriting big-ticket deals let ADLC and other leasing companies benefit from economies of scale. In order to comply with its internal operating policies to underwrite big-ticket deals, the company had to enlarge its capital base. As BAY has a policy to pursue a universal banking concept, BAY Group and one foreign shareholder (Deutsche Investitions-und Entwicklungsgesellschaft mbH: DEG) have injected Bt235 million of new capital into ADLC in 2004, increasing paid-up capital from Bt470 million to Bt705 million. The shareholding portion of the BAY Group rose from 40.3% in 2003 to 56.5% in 2004.

▪ **Divestment by IFC and KDLC**

IFC has a policy to invest and lend to organizations in developing countries to support development in such countries. In general, IFC’s policy limits its investment period to no longer than 10 years. However, IFC has maintained its investment in ADLC for about 14 years because ADLC still needed financial support during the financial crisis. As of March 2005, the two foreign founders, IFC and KDLC, sold their shares to BAY. BAY and its subsidiaries currently hold a stake of approximately 76% of ADLC.

Chart 1: Outstanding Loan Portfolio Compositions as of 31 December 2004



Source: ADLC

After the crisis, ADLC’s outstanding loans grew by 104% from Bt1,760 million at the end of 1999 to Bt3,599 million at the end of 2004. The composition of its portfolio changed after the crisis. The proportion of general manufacturing

Table 1: Major Shareholders of ADLC as of July 2005

Name	% of Shares
Bank of Ayudhya PLC	62.07
Deutsche Investitions-und Entwicklungsgesellschaft mbH (DEG)	10.00
Ayudhya Insurance PLC	8.51
Ayudhya Investment & Trust PLC	5.11
Kookmin Bank	3.55
Netherlands Development Finance Company	3.26
Others	7.50

Source: ADLC

INDUSTRY ANALYSIS

▪ *Alternative funding source for SMEs*

After the 1997 financial crisis, the number of small- and medium-sized enterprises (SMEs) was continuously increasing through government promotional programs. Normally, SMEs face more difficulty raising funds from traditional financial sources such as commercial banks compared with large enterprises, due to the shorter operational track record and/or lack of sufficient reliable audited financial statements. Normally, a lessor will consider the cash flow generated from the leased assets to evaluate the ability of the lessee to service the lease rental. Rather than invest entirely in machinery or equipment when starting a business and acquiring the equipment, an SME as lessee will be able to use its limited funds as working capital. Moreover, for tax purposes, cash purchase or hire purchase payments will be deducted as depreciation expenses over the useful life of the assets (at least five years) while the lease rental will be deductible as an expense over the contract term which may be less than five years. Lessees will benefit from accelerating deductible expenses which will lower taxable income and tax expense.

▪ *Limited competition amidst few operators*

Though the industrial machinery and equipment leasing business has been operational in Thailand for more than 20 years, the volume is considered low. Lease volume accounted for only around 1% of national private investment in 2003, whereas the three largest leasing markets, US, Germany and Japan, had penetration rates of 31.1%, 15.4%, and 8.7% of their national private investment respectively.

Of the 22 leasing companies that are members of the Thailand Leasing Association (TLA), only a few companies concentrate on industrial machinery and equipment leasing. Many leasing firms that use the word “leasing” in their names mostly provide hire purchase loans, which are automobile hire purchases. Machinery and equipment leases can be granted to a variety of products and need a different credit risk analysis. For machinery and equipment leases, the lessees are usually corporations in different industries, while automobile hire purchase lessees are mostly individuals. The credit risk analysis procedures for applicants are different but will include at least an assessment of the industry’s prospects, a cash flow analysis, and liquidity analysis of the leased asset in the event disposition is needed. Commercial bank lenders

rely on mortgage securities and standard procedures to grant loans, whereas equipment leasing has the flexibility of being assessed and structured, based on cash flows of the lessee and the liquidity of the leased assets.

BUSINESS ANALYSIS

▪ *Strong market position in equipment leasing*

ADLC is a major operator in the equipment leasing industry in Thailand. The company’s outstanding loans have consistently grown after the financial crisis. As of December 2003, ADLC ranked second among seven major equipment leasing operators in TRIS Rating’s database in terms of outstanding leasing loans. Among seven leasing operators, ADLC’s market share, measured by the outstanding leasing loans, decreased from 19.8% in 1999 to 16.5% in 2003. However, with its long track record and the ability for tailor-made services to meet customer needs, ADLC should be able to maintain its strong market position in the medium term.

▪ *Experienced management team and efficient operating system*

ADLC’s current Chief Executive Officer gained extensive experience working at KDLC for 20 years. The founding shareholders helped set the operating system, risk management system, and operational guidelines to assess the credit risks of the lessee. ADLC’s management also learned to customize leasing programs to meet customers’ needs, providing a meaningful point of differentiation.

▪ *Strong support from major shareholders*

Major shareholders have provided financial and non-financial support to ADLC since its inception. Though the major foreign shareholders have divested their shares, ADLC learned enough about the business during 14 years of support to efficiently run the business by itself. From 2005 onward, as BAY owns 76% of ADLC shares, ADLC will be able to leverage BAY’s extensive branch network and large customer base to expand its loan portfolio.

ASSET QUALITY

▪ *Nature of business and deal structure reduce losses from high credit risk customers*

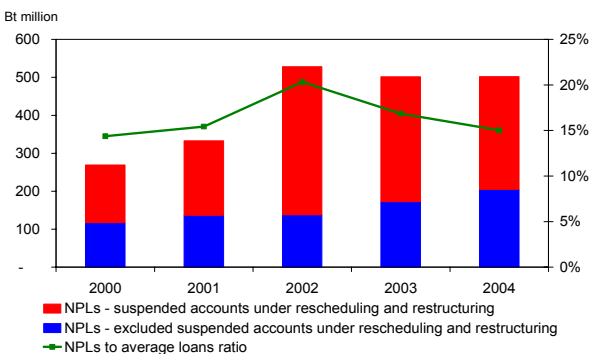
Naturally, the credit risk of ADLC’s customers is higher than commercial bank corporate clients. However, ADLC’s strategy is to lower the probable losses from higher

customer credit risk. The title of the leased assets belongs to the lessor. While the lessor is permitted to change the lessee immediately after the lessee misses payment, in practice, the company uses this permission to force the lessee to pay the rental fees over the contract term as the lessee's business often absolutely depends on the leased assets. Moreover, a deposit, assignment of payment, and buy-back guarantee from suppliers will help mitigate losses from high credit risk lessees to some extent.

▪ **High non-performing loans from a few large contracts**

As of December 2004, ADLC's non-performing loans (NPLs -- overdue by more than three months) were 15.0% of average loans, down from 20.3% and 16.9% at the end of 2002 and 2003, respectively. The delinquency rate of ADLC is quite high when compared with automobile hire purchase companies due to ADLC's small customer base. Most of ADLC's NPLs were classified as doubtful losses, which included suspended accounts under rescheduling and restructuring. These doubtful losses accounted for 74%, 66%, and 59% of NPLs during 2002-2004, respectively. The doubtful loss accounts comprise a few accounts affected by the crisis. Actually, the suspended accounts under rescheduling and restructuring could be classified as normal accounts as they have continuously made payments after their obligations were rescheduled or restructured. However, ADLC will continue to classify these loans as NPLs and will monitor the loans for 1-2 years after restructuring. Once ADLC has enough confidence in the payment performances of the lessees, the loans will be reclassified to normal status.

Chart 2: ADLC's NPLs During 2000-2004



Source: ADLC

PROFITABILITY

ADLC recorded loss during its first two years of operation (1991-1992). After that, even during the crisis, ADLC reported net income until 2003, when the company set a special Bt90 million provision.

▪ **Low profitability due to sizable NPLs in portfolio**

ADLC concentrates on special machinery and equipment leases, which required knowledge to underwrite or structure deals to match lessee's needs. ADLC can charge a premium rate over normal equipment leases, setting a 5% minimum spread. The average lease rate is 10%. However, because of a high portion of NPLs that the company has not yet written off, profitability remains low. The return on assets ratio stayed in the range of 0.9%-1.6% during 1999-2004, except for a report of -1.5% in 2003 when the company reported a net loss.

▪ **Sustain low operating cost and enhanced profitability from big-ticket deal**

With an efficient operating system and relatively large average contract size, ADLC benefits from economies of scale, which helps it control operating costs. The ratio of operating expenses to total income has stayed at an average of 15% during 2001-2004. A Bt1,920 million and 3-year structured operating lease contract with Advanced Data Network Communication Co., Ltd. (ADC), a joint venture between Advanced Info Service PLC and TOT PLC, was successfully closed in early 2005. This deal will generate sizable revenue to ADLC. If this deal is as successful as planned, ADLC's profitability will benefit over the next three years. TRIS Rating expects that the company will be able to maintain a low operating cost ratio.

LIQUIDITY/FUNDING

Most of ADLC's assets are financial lease loans. After the crisis, the ratio of total loans to total assets consistently increased as the portfolio expanded during the economic recovery period. The total loans to total assets ratio increased from 78.3% at the end of 1999 to 96.3% at the end of 2004.

▪ **Shareholder support will likely be a source of reliable liquidity**

Since its inception, ADLC has balanced its financing needs by seeking funds both by borrowing and by raising capital. During the

crisis, the company's foreign shareholders helped the company solve its liquidity problem by granting long-term loans to refinance its foreign short-term borrowings. As of March 2005, ADLC had no foreign debts but borrowed a significant portion of its total debt from BAY. Total borrowings were Bt2,098.6 million of which Bt1,261.2 million (58%) was from BAY. ADLC is trying to diversify its funding sources to lower its financing costs. The company plans to issue debentures to secure a long-term fixed funding before interest rates rise further.

▪ **Limited liquidity risk due to strict criteria**

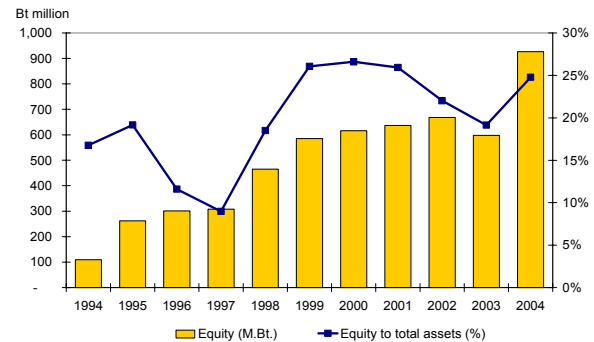
After a bad experience in 1997 crisis, ADLC has set strict criteria to mitigate its liquidity risk and currency risk. The company carefully manages its asset-liability mix by maintaining a minimum excess duration of assets over liabilities. Moreover, ADLC set a minimum liquidity level, matching floating rate lease contracts with floating rate funding, and limits exposure to foreign exchange rates.

CAPITAL

With the support of its shareholders, ADLC's capital base has consistently increased through new capital injections. ADLC started operations with Bt40 million in paid-up capital in 1991, which was increased to Bt100 million the following year. As the economy was booming, ADLC doubled its portfolio in 1995 with funding from both borrowings and new equity. Paid-up capital increased to Bt250 million in 1997. ADLC faced the same difficulties during the crisis as its peers; however, its shareholders helped to refinance its debts and also injected Bt150 million and Bt70 million in new capital in 1998 and 1999, respectively, to provide a cushion for possible loan losses.

The ratio of shareholder's equity to total assets jumped from 9.0% in 1997 to 18.5% in 1998 and to 26.1% in 1999, as a result of both the shrinking loan portfolio and the capital increases. ADLC maintained its paid-up capital at Bt470 million during 1999-2003. After the crisis, ADLC expanded its portfolio mainly through borrowings. Though the equity base was growing from retained earnings, it was not rapid enough to fund the rapid loan expansion. This caused the ratio of shareholders' equity to total assets to fall continuously, 26.6% in 2000 to 25.9%, 22.0% and 19.2% in 2001, 2002 and 2003, respectively. By 2004, the prospect of future big-ticket deals and a conservative policy to maintain an adequate cushion to absorb possible credit losses caused the company to increase its capital. BAY realizes that ADLC will act as its arm in the leasing business as part of its universal banking policy; therefore, BAY and its subsidiaries injected Bt235 million in new paid-up capital in 2004. This capital injection strengthened ADLC's shareholders' equity to total assets ratio to 24.5% at the end of 2004.

Chart 3: ADLC's Shareholders' Equity and Equity to Total Assets



Source: ADLC

Financial Statistics and Key Financial Ratios

Unit: Bt million

	Year ended 31 December				
	2004	2003	2002	2001	2000
Total assets	3,738	3,121	3,034	2,454	2,316
Total loans net of unearned interest income	3,599	3,083	2,870	2,327	1,987
Allowance for loan losses	264	302	214	178	178
Short-term borrowings	1,371	756	571	858	294
Long-term borrowings	703	1,031	1,230	630	1,158
Shareholders' equity	926	597	668	637	616
Net interest income	113	84	75	55	58
Non-interest income	14	7	23	19	37
Operating expenses	33	31	28	29	30
Net income	30	(47)	32	21	31

Key Financial Ratios

Unit: %

	Year ended 31 December				
	2004	2003	2002	2001	2000
Profitability					
Net-interest income/average assets	3.28	2.72	2.73	2.29	2.55
Net-interest income/total income	50.67	42.25	36.39	28.65	26.14
Operating expenses/total income	14.81	15.72	13.69	15.12	13.33
Operating profit/average assets	0.88	(0.97)	1.22	1.33	1.81
Return on average assets	0.88	(1.53)	1.15	0.86	1.34
Return on average equity	3.97	(7.45)	4.83	3.29	5.09
Asset Quality					
Non-accrual loans/average loans	15.02	16.88	20.33	15.43	14.37
Loan loss provision/average loans	1.89	3.13	1.46	1.14	8.98
Allowance for loan losses/total loans	7.33	9.78	7.47	7.63	8.98
Leverage					
Shareholders' equity/total assets	24.78	19.15	22.02	25.94	26.60
Shareholders' equity/total loans	25.74	19.38	23.28	27.36	31.01
Total liabilities/total liabilities+shareholders' equity	75.22	80.85	77.98	74.06	73.40
Liquidity					
Short-term borrowings/total liabilities	48.75	29.97	24.14	47.21	17.29
Total loans/total assets	96.27	98.80	94.60	94.81	85.78
Total loans/total borrowings	173.55	172.48	159.34	156.33	136.87

Rating Symbols and Definitions

TRIS Rating uses letter rating symbols for announcing credit rating results for long-term debt instruments. Ratings range from AAA, the highest rating, to D, the lowest rating. The definitions are:

AAA	the highest rating with smallest degree of credit risk, extremely strong capacity to pay interest and repay principal on time, and unlikely to be affected by adverse changes in business, economic or other external conditions.
AA	the debt instrument with very low degree of credit risk, very strong capacity to pay interest and repay principal on time, but somewhat more susceptible to the adverse changes in business, economic, or other external conditions than the AAA rated issues.
A	the debt instrument with low credit risk, strong capacity to pay interest and repay principal on time, but more susceptible to the adverse changes in business, economic or other external conditions than debt in higher rated categories.
BBB	the debt instrument with moderate credit risk, moderate capacity to pay interest and repay principal on time, but more vulnerable to adverse changes in business, economic or other external conditions which is likely to weaken the capacity to pay interest and repay principal than debt in higher rated categories.
BB	the debt instrument with high credit risk, less than moderate capacity to pay interest and repay principal on time, and can be significantly affected by adverse changes in business, economic or other external conditions with lower creditors' protection than provided by higher ratings.
B	the debt instrument with very high credit risk, low capacity to pay interest and repay principal on time. Adverse changes in business, economic or other external conditions would lead to lack of ability or willingness to pay interest and repay principal.
C	the debt instrument with highest risk of default than debt in higher rated categories, significant inability to pay interest and repay principal on time and dependent upon favourable business, economic or other external conditions in order to meet its obligations.
D	the debt instrument in which payment is in default.

The ratings from AA to C may be modified by the addition of a plus (+) or minus (-) sign to show relative standing within a rating category.

The ratings assigned by TRIS Rating are local currency ratings; they reflect the Thai issuers' ability to service their debt obligations, excluding the risk of convertibility of the Thai baht payments into foreign currencies. Therefore, the ratings are not capped by the (foreign currency) sovereign ceiling of Thailand, which are assigned by international credit rating agencies.

TRIS Rating also assigns "Rating Outlooks" to reflect the potential direction of a company's credit ratings over the medium to long term. In formulating these outlooks, TRIS Rating will consider the prospects for the rated company's industry, as well as business conditions that might have an impact on its fundamental creditworthiness. Rating outlooks will be announced in conjunction with company credit ratings, and new outlooks will be generated as circumstances warrant. In most cases, outlook assigned to a company will apply to all debt obligations issued by the company.

The categories for "Rating Outlooks" are as follows:

Positive	the rating may be raised
Stable	the rating is not likely to be changed
Negative	the rating may be lowered
Developing	the rating may be raised, lowered or remain unchanged

For subscription information, contact

TRIS Rating Co., Ltd., Office of the President, Tel: 0-2231-3011 ext 500

Silom Complex Building, 24th Floor, 191 Silom Road, Bangkok 10550, Thailand, <http://www.trisrating.com>

© Copyright 2005, TRIS Rating Co., Ltd. All rights reserved. Any unauthorized use, disclosure, copying, republication, further transmission, dissemination, redistribution or storing for subsequent use for any purpose, in whole or in part, in any form or manner or by any means whatsoever, by any person, of the credit rating reports or information is prohibited. The credit rating is not a statement of fact or a recommendation to buy, sell or hold any debt instruments. It is an expression of opinion regarding credit risks for that instrument or particular company. The opinion expressed in the credit rating does not represent investment or other advice and should therefore not be construed as such. Any rating and information contained in any report written or published by TRIS Rating has been prepared without taking into account any recipient's particular financial needs, circumstances, knowledge and objectives. Therefore, a recipient should assess the appropriateness of such information before making an investment decision based on this information. Information used for the rating has been obtained by TRIS Rating from the company and other sources believed to be reliable. Therefore, TRIS Rating does not guarantee the accuracy, adequacy, or completeness of any such information and will accept no liability for any loss or damage arising from any inaccuracy, inadequacy or incompleteness. Also, TRIS Rating is not responsible for any errors or omissions, the result obtained from, or any actions taken in reliance upon such information.