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Fitch Affirms KCE Electronics at 'A-(tha)'; Outlook Stable

Fitch Ratings - Bangkok - 02 Jul 2023: Fitch Ratings (Thailand) Limited has affirmed KCE Electronics Public Company Limited's National Long-Term Rating at 'A-(tha)'. The Outlook is Stable.

The rating affirmation reflects Fitch's expectation that KCE's financial profile will remain strong and commensurate with the rating in the medium term, despite weaker earnings in 2023. KCE's currently low financial leverage should provide some headroom. We forecast KCE's EBITDA net leverage to increase to about 1.9x in 2025, driven by capex for the Rojana project, and to fall to around 1.0x in 2026.

Key Rating Drivers

Revenue to Drop in 2023: Fitch expects KCE's 2023 revenue to drop by around 5%-6% in 2023, against a 23.6% increase in 2022. Automotive suppliers - KCE's main customers - are likely to reduce printed circuit board (PCB) orders in 2023 to lower the risk of overstocking while heading into an economic slowdown. Slow global economic growth and aggressive stock building in the past two years have reversed the favourable PCB supply-demand environment, resulting in high inventory in 2H22 and 1H23.

Maintain Margin in 2023: KCE can maintain its EBITDA margin at 17%-18% in 2023 despite lower revenue, in Fitch's view. The impact on the margin from lower sales should be offset by the lower raw material and energy costs in 2023. An increase in high-margin, multi-layered automotive PCB product sales should support the margin improvement over 2024 and 2025. KCE's EBITDA margin declined to 17.8% in 2022 (2021: 22.4%), due largely to a surge in the copper price and energy costs in 2H22.

Capex Flexibility: KCE has cut 2023 capex to around THB600 million (2022: THB1 billion), in response to the weak PCB demand. The company has also delayed the construction of the Rojana project, a greenfield project with capacity of up to 1 million square feet a month, to 2024, in line with Fitch's expectation that PCB orders will start to recover in 2024. Fitch has estimated total capex for the Rojana project of around THB7.3 billion in 2024 and 2025.

Higher, Yet Healthy, Leverage: KCE's EBITDA net leverage is likely to rise in 2024-2025 on high investment in the Rojana project. Fitch believes that KCE's low EBITDA net leverage of 0.8x at end-2022 should be able to absorb the project investment while keeping leverage commensurate with the rating. We forecast net leverage during the construction period to peak at around 1.9x in 2025, before falling to around 1.0x in 2026 when the new plant starts operating.

Leading Auto PCB Producer: KCE's rating reflects its leading position in the automotive PCB business, which has longer product cycles and deeper customer engagement, providing higher entry barriers and a wider EBITDA margin than those of consumer electronic PCB. The company is one of the world's top-10 automotive PCB makers, with revenue market share of 3%-5%.

Long-Term Growth Opportunities: Fitch believes that the automotive PCB industry remains poised for long-term growth, underpinned by global expansion in vehicle production, particularly electric vehicles, and increasing penetration of electronics content in automobiles, despite near-term economic cyclicity. New applications, such as safety, driver assistance and infotainment systems, which were previously available only in luxury cars, are becoming standard in the mass middle market.

Reduced Customer Concentration: KCE's expansion into the high-density interconnect (HDI) segment, including non-automotive products, is likely to reduce customer concentration gradually over the medium term. The company's five largest customers contributed about 58% of its total PCB revenue in 2022, declining over the past 10 years from about 65% in 2010.

Currency Volatility: KCE is exposed to foreign-exchange fluctuations, resulting in a volatile EBITDA margin. KCE is an exporter and its earnings generally hurt when the Thai baht appreciates, as around 80%-90% of its revenue is in US dollars and euros, while around 50%-60% of costs are in baht, and mostly unhedged.

Derivation Summary

KCE's business profile is moderate relative to that of nationally rated Thai peers, but its financial profile is stronger. KCE's business and financial profiles are comparable with those of Polyplex (Thailand) Public Company Limited (PTL, A-(tha)/Stable), one of the top-10 polyester film producers in the world by revenue.

PTL operates in a higher-risk industry, as most of its products are standard films that are considered a commodity and face intense competition. KCE focuses on automotive PCBs, a niche segment with higher barriers to entry. However, PTL has more geographically diversified operations and a broad customer base. Both companies have low financial leverage, with EBITDA net leverage of below 1.5x. The ratings are therefore the same.

Eastern Polymer Group Public Company Limited (EPG, A-(tha)/Stable) and KCE have businesses that supply the automotive industry, but different product offerings. EPG is a manufacturer of polymer and plastic automotive parts and accessories for utility trucks, which account for about 50% of its total revenue.

EPG has a more diversified customer base across multiple end-user segments than KCE, given its diversified core businesses in thermal insulation and food and beverage plastic packaging. KCE and EPG have comparable operating scales, but KCE generally has better EBITDA and free cash flow margins. Their ratings are the same due to their comparable business profiles and similarly low financial leverage.

Key Assumptions

Fitch's Key Assumptions Within Our Rating Case for the Issuer:

- Revenue to decline by 5%-6% in 2023 (2022: +24%), due mainly to automotive suppliers lowering PCB orders to reduce their stocks; revenue to recover by 5% in 2024.
- Revenue to increase at 19%-25% a year in 2025-2026, supported by a strong order for HDI products at the new Rojana plant.
- EBITDA margin to be flat at around 17%-18% in 2023, before gradually improving from 2024 on higher capacity utilisation and a higher proportion of sales from high-margin, special-graded PCB products.
- Total capex plan for the Rojana project and technological upgrade of around THB8 billion during 2023-2025 (2022: THB1 billion).
- Maintain dividend payout ratio of 80% (2022: 82%).

RATING SENSITIVITIES

Factors that could, individually or collectively, lead to positive rating action/upgrade:

- We do not expect an upgrade in the medium term unless KCE achieves a substantial increase in its operating scale and a more diverse customer mix, while maintaining EBITDA net leverage below 2x for a sustained period.

Factors that could, individually or collectively, lead to negative rating action/downgrade:

- Lower cash flow or higher investments than Fitch expects or acquisitions leading to EBITDA net leverage above 1.5x on a sustained basis;
- Decline in the operating EBITDA margin to below 13% for a sustained period;
- A weakening in the company's market position or loss of key customers.

Liquidity and Debt Structure

Manageable Liquidity: KCE had THB3.8 billion in debt at end-2022. Debt maturing in 2023 is THB2.9 billion, of which THB2.2 billion is short-term debt. Most of the short-term debt is packing credits. These are bank loans for financing export activity and they can be rolled over. Liquidity is supported by a cash balance of THB1.1 billion and uncommitted revolving facilities of THB15.7 billion and USD67 million at end-2022. Additional capex for capacity expansion is likely to be funded by internal cash flow generation and new long-term loans from banks.

Issuer Profile

KCE is one of the ten-largest automotive PCB operators in the world by revenue. Automotive PCB accounted for around 80% of its PCB sales. KCE exports its PCB products globally, with Europe

contributing 41% of PCB revenue in 2022, the US 19% and Asia 40%.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

Fitch Ratings Analysts

Obboon Thirachit

Senior Director

Primary Rating Analyst

+66 2 108 0159

Fitch Ratings (Thailand) Limited Park Ventures, Level 17 57 Wireless Road, Lumpini Bangkok 10330

Lertchai Kochareonrattanakul

Senior Director

Secondary Rating Analyst

+66 2 108 0158

Nitin Soni

Senior Director

Committee Chairperson

+65 6796 7235

Media Contacts



Leslie Tan

Singapore

+65 6796 7234

leslie.tan@thefitchgroup.com

Rating Actions

ENTITY/DEBT	RATING		RECOVERY	PRIOR
KCE Electronics Public Company Limited	Natl LT	A-(tha) 	Affirmed	A-(tha) 

RATINGS KEY OUTLOOK WATCH

POSITIVE



RATINGS KEY OUTLOOK WATCH

NEGATIVE	⊖	◊
EVOLVING	◊	◆
STABLE	○	

Applicable Criteria

[Corporate Rating Criteria \(pub.28 Oct 2022\) \(including rating assumption sensitivity\)](#)

[National Scale Rating Criteria \(pub.22 Dec 2020\)](#)

[Sector Navigators: Addendum to the Corporate Rating Criteria \(pub.12 May 2023\)](#)

Applicable Models

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

Corporate Monitoring & Forecasting Model (COMFORT Model), v8.1.0 [\(1\)](#)

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