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

Fitch Ratings - Bangkok - 07 Aug 2024: 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 over the next two years. KCE's improving earnings and its ample rating headroom due to currently low financial leverage should provide financial flexibility to support higher capex. We forecast KCE's EBITDA net leverage to increase to about 1.5x in 2025, driven by capex for the Rojana project, and to fall to around 1.1x in 2026.

Key Rating Drivers

Slow Revenue Recovery: Fitch forecasts slow revenue growth of 4%-5% a year for KCE in 2024-2025, following a decline of 11% in 2023. We expect the pressure from inventory build-up at automotive suppliers to ease, while demand for special-grade printed circuit boards (PCB), including high-density interconnect (HDI) products, should remain strong. The increasing use of electronics such as 5G, advanced driver assistance system (ADAS), and light detection and ranging (LIDAR) in vehicles should support medium-term demand for KCE's PCB products.

Improving Margin: We forecast KCE's EBITDA margin to improve slightly to 17%-18% in 2024, from 16.6% in 2023 (1Q24: 18.9%). The improvement is likely to be driven by more efficient production, with increasing automation resulting in fewer employees. In the medium term, KCE's EBITDA margin improvement should be supported by a rise in sales of higher-margin, multi-layer automotive PCBs, coupled with better utilisation from recovering demand, as well as a declining

trend in electricity tariffs.

Ample Leverage Headroom: Fitch believes KCE's low EBITDA net leverage of 0.2x at the end-2023 should provide sufficient capacity to absorb an increase in investment while maintaining leverage levels consistent with the rating. KCE's EBITDA net leverage is expected by Fitch to increase in 2025-2026 due to significant investment in the Rojana project. We forecast EBITDA net leverage to peak at about 1.5x in 2025 during the construction of Rojana project, then decline to around 1.1x in 2026 when the new plant starts operation.

High but Flexible Capex: KCE's capex is likely to increase to around THB8.8 billion over 2024-2026. This is mainly to support the construction of Rojana project (THB7.3 billion), a greenfield development with a capacity of up to 1 million square feet per month; the balance (THB1.5 billion) will be mainly for efficiency improvements and maintenance.

Meanwhile, total capex will depend on actual demand because around THB 3.8 billion of capex will be allocated to machinery and manufacturing support, which can be deferred if demand is weaker than expected by KCE. The company has postponed the construction of Rojana project to 2025 from 2024.

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 consumer electronics PCBs. 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 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 that were previously available only in luxury cars, such as safety, driver assistance and infotainment systems, are becoming standard in the mass middle market.

Reduced Customer Concentration: KCE's expansion into the 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 57% of its total PCB revenue in 2023, 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 85%-95% of its revenue is in US dollars and euros, while around 50%-60% of costs are in baht and mostly unhedged.

Derivation Summary

KCE and Eastern Polymer Group Public Company Limited (EPG, A-(tha)/Stable) have businesses that supply the automotive industry but with 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 margin. Their ratings are the same due to their comparable business profiles and similarly low financial leverage.

KCE rating is higher than SCGJWD Logistics Public Company Limited's (BBB+(tha)/Stable) 'bbb(thai)' Standalone Credit Profile (SCP). KCE's business profile is stronger than SCGJWD, as KCE's business has lower competition given the high barrier to entry in automotive PCB business, compared with SCGJWD's logistic service industry. Moreover, KCE has stronger financial profile due to lower financial leverage. This results in SCGJWD's SCP being rated two notches below KCE's National Long-term Rating.

SCGJWD's National Rating incorporates a one-notch uplift from its 'bbb(thai)' SCP due to the moderate support incentives with its parent, The Siam Cement Public Company Limited (A(thai)/Stable).

KCE has weaker business profile than SCG Packaging Public Company Limited (SCGP, A(thai)/Stable, SCP: a(thai)), a leading paper-backed packing business in ASEAN. SCGP has much larger revenue and EBITDA. It also has a leading position in the paper-based packaging business in south-east Asia. KCE has lower financial leverage, but this is not enough to offset its weaker business profile, resulting in KCE being rated one notch below SCGP.

Key Assumptions

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

- Revenue growth of about 4%-5% a year in 2024 and 2025 (2023: 11% decline) from decreasing pressure from inventory built up, while demand for special grade PCB, including HDI products, to stay strong;
- Revenue to increase by 20%-25% in 2026, supported by additional HDI capacity at the new Rojana plant;
- EBITDA margin to improve to around 17%-18% in 2024 (2023: 16.6%) on higher capacity utilisation, a higher proportion of sales from high-margin, special-graded PCB products, and efficiency improvement measures;
- Total capex plan for the Rojana project, and production efficiency improvement and maintenance of around THB8.8 billion during 2024-2026 (2023: THB400 million);
- Maintain dividend payout ratio of 80%.

RATING SENSITIVITIES

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

- We do not foresee an upgrade over the rating horizon of the next few years, but an upgrade in the longer term is possible if KCE successfully expands its business scale and diversifies its customer mix.

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 being above 1.5x on a sustained basis;
- A 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 total debt of THB1.4 billion at end-1Q24. Debt maturing in the next 12 months is THB927 million, of which THB510 million is short-term debt, mostly packing credits, which are bank loans for financing export activity and can be rolled over. Liquidity is supported by a cash balance of THB2.1 billion which should be sufficient to meet the obligation. 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 10-largest automotive PCB operators in the world by revenue. Automotive PCB accounted for around 83% of its PCB sales. KCE exports its PCB products globally, with Europe contributing 48% of PCB revenue in 2023, the US 24% and Asia 28%

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.

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Rating Actions

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

RATINGS KEY OUTLOOK WATCH

POSITIVE



NEGATIVE



RATINGS KEY OUTLOOK WATCH

EVOLVING ◉ ◆

STABLE ○

Applicable Criteria

[Corporate Rating Criteria \(pub.03 Nov 2023\) \(including rating assumption sensitivity\)](#)

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

[Sector Navigators – Addendum to the Corporate Rating Criteria \(pub.21 Jun 2024\)](#)

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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