DOUBLE A (1991) PLC

No. 144/2017

8 November 2017

Company Rating: BBB-

Outlook: Negative

Company Rating History:

Date	Rating	Outlook/Alert
25/11/16	BBB-	Negative
26/10/15	BBB-	Stable
12/09/13	BBB	Stable
21/08/12	BBB	Negative
16/05/08	BBB	Stable
09/11/07	BBB	Alert Developing
28/02/06	BBB	Stable
16/11/05	BBB	Alert Developing
20/10/04	BBB	Stable

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Rating Rationale

TRIS Rating affirms the company rating of Double A (1991) PLC (DA) at "BBB-", and also affirms the "negative" outlook of DA. The "BBB-" rating reflects DA's position as one of the leading printing & writing (P&W) paper producers in Thailand, its fully integrated pulp and paper mills, and the strong brand name of "Double A" products. These strengths are partially offset by the inherent volatility of the pulp and paper industry, DA's exposure to foreign exchange risk, stagnant demand for P&W paper due to a widespread slowdown in the global economy and a shift in consumer behavior towards digital media, as well as concerns about some related-party transactions.

Founded in 1989, DA is the leading P&W paper producer in Thailand. It is a subsidiary of Double A Holding Limited., which has the Dumnernchanvanit family as the major shareholder. As of September 2017, Mr. Yothin Dumnernchanvanit and affiliated parties were the ultimate shareholders, holding a 87.8% of stake in DA. DA currently owns and operates five paper mills, with a total design capacity of 1,045,000 tonnes per annum (tpa). Paper production capacity doubled after the start-up of the third paper mill (APM3) in Thailand in November 2012 and the acquisition of the Alizay paper mill (Alizay) in France in January 2013. DA spent about Bt5,000 million for APM3 and about Bt1,400 million for Alizay. Paper sales account for about 90% of the company's annual sales, followed by sales of wood chips (7%), pulp (2%), as well as revenue from services (1%).

DA's competitive edge stemmed from the fully integrated pulp and paper operations in Tha Toom district, Prachinburi province. DA has its own pulp production capacity of 427,000 tpa. The company produces only short-fiber pulp, and uses nearly all the pulp produced as the raw material for the company's Thai paper mills. The Thai paper mills have a total design capacity of 745,000 tpa. The integration of the paper mills with the pulp mills creates synergy and enhances DA's cost competitiveness.

In contrast to the Thai paper mills, Alizay lacks synergy because it operates only a paper mill in France. As a result, the cost of paper produced at Alizay is higher than that at the Thai paper mills. In addition, an economic slowdown in Europe and a shift in consumer behavior towards digital media have made Alizay unable to boost production enough to reach advantageous economies of scale. Alizay has faced operating losses since commercialization in 2013. Earnings before interest, tax, depreciation, and amortization (EBITDA) was negative at Bt105 million in the first half of 2017.

DA's paper markets are geographically diverse and it has a strong distribution network covering more than 100 countries worldwide. Sales to the Thai (domestic) market comprised almost 30% of total sales. About 50% of sales came from other markets in Asia, 10% from markets in Europe, and 10% from other countries. As about 70% of total sales come from international markets, DA is inevitably exposed to foreign exchange risk.

Profitability has gradually improved after a tumble during 2014 and 2015. The operating margin (operating income before depreciation and amortization as percentage of sales) slumped to 5.9% in 2014 and 3.3% in 2015, compared with the past levels of above 10%. The significant fall was mainly due to machinery problems. The operating margin rose to 8.2% in 2016 and 12.2% in the first half of

2017. The recent rises were mainly attributed to the improvement plan obtained through the advice of the third party advisors. The improvement plan involves several key areas such as the enhancement of production efficiency and a focus on core markets and premium products. The overall cost of production fell after DA revised its production plan. The company reduced production at the high-cost Alizay paper mill and boosted production at the Thai paper mills instead. By concentrating on strategic markets, rather than penetrating many new markets, operating expenses fell. A reduction in the number of product lines reduced the machinery problems. EBITDA recovered to Bt2,107 million in 2016, from Bt1,050 million in 2015, while funds from operations (FFO) edged up to Bt1,124 million in 2016, from Bt867 million in 2015. EBITDA and FFO continued to improve in the first half of 2017, rising to Bt1,457 million and Bt1,443 million, respectively. Cash flow protection also recovered as profitability restored. The FFO to total debt ratio rose to 9.3 times in the first half of 2017, from a bottom of 2.9 times in 2014. The total debt to EBITDA ratio dropped to 8.9 times in the first half of 2017, from a peak of 21.2 times in 2015. Despite the improvements, cash flow protection remained weaker than the level commensurate with the rating.

DA plans to sell Alizay to Double A Holding Limited, its parent company. The sale, or spinoff, is expected to occur by the end of 2017. The selling price is currently under review, but it should be approximately Bt2,000 million. DA expects no significant gains or losses on the sale of Alizay. DA plans to pay a dividend to Double A Holding Limited to fund the purchase of Alizay. As a consequence, leverage should increase after the spinoff. In addition, shareholders' equity of DA will decrease once the revaluation surplus for Alizay's assets, worth about Bt1,400 million, is removed. TRIS Rating assumes the debt to total capitalization ratio will rise to about 65% from 53.6% as of June 2017. TRIS Rating forecasts the operating margin will rise to 14%-15%, after the deconsolidation of Alizay and a continuation of the efficiency improvement plan. EBITDA will rise to Bt3,000-Bt3,500 million per annum, while FFO will rise to Bt2,000-Bt2,500 million per annum. Over the next three years, TRIS Rating projects the FFO to total debt ratio and the total debt to EBITDA ratio will range from 10%-13% and 5-7 times, respectively, given an assumption that DA will provide no further support to Alizay. FFO, forecast at Bt2,000-Bt2,500 million per annum, should cover all maintenance capital expenditures of about Bt1,000 million per annum and annual long-term bank debt repayments of about Bt600 million over the next three years. February 2019 is the redemption date for Bt2,350 million worth of outstanding debentures. DA generally refinances the debentures before they come due. TRIS Rating expects DA will manage the refinancing risks prudently.

Rating Outlook

The "negative" outlook reflects the fact that DA's profitability and cash flow generating ability are on the path of recovery, but remain below the level commensurate with the rating. The outlook could be revised back to "stable" if the improvements in profitability and cash flow protection continue, as expected and on a sustainable basis. The company rating will also be influenced by the company rating of National Power Supply PLC (NPS), which has the same ultimate shareholder, according to TRIS Rating's group rating methodology. Any change in the company rating of NPS would affect the company rating of DA.

Double A (1991) PLC (DA)

Company Rating:	BBB-
Rating Outlook:	Negative

Financial Statistics and Key Financial Ratios*

Unit: Bt million

	Jan-Jun 2017	------------------ Year Ended 31 December -------------- 2016	2015	2014	2013
Sales	12,652	26,121	23,370	22,963	17,874
Gross interest expense	498	1,171	1,232	1,298	1,216
Net income from operations	(381)	(1,346)	(2,387)	(1,116)	(561)
EBITDA	1,457	2,107	1,050	2,268	2,580
Funds from operations (FFO)	1,443	1,124	867	677	2,125
Capital expenditures	344	950	1,244	1,171	3,260
Total assets	42,277	42,692	43,109	45,170	44,518
Total debt	19,901	20,530	22,308	23,185	22,563
Shareholders' equity	17,253	17,352	16,142	17,084	17,084
Operating income before depreciation and amortization as % of sales	12.24	8.18	3.35	5.87	10.22
Pretax return on permanent capital (%)	(1.17)**	(1.04)	(3.57)	(0.11)	1.51
Earnings before interest, tax, depreciation, and amortization (EBITDA) interest coverage (times)	2.93	1.80	0.85	1.75	2.12
FFO/Total debt (%)	9.27**	5.48	3.89	2.92	9.42
Total debt/capitalization (%)	53.56	54.20	58.02	57.58	56.91
Total debt/EBITDA (times)	8.93**	9.74	21.24	10.22	8.75

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

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