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EASTERN PRINTING PLC

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Company Rating: BBB

Outlook: Stable

Company Rating History:

Date	Rating	Outlook/Alert
01/12/15	BBB	Stable

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Rating Rationale

TRIS Rating affirms the company rating of Eastern Printing PLC (EPCO) at "BBB". The rating reflects EPCO's solid market position and long-established track record in the printing industry, the profitability of the core business albeit with meager prospects for growth, diversification into the power business, and more predictable cash flows derived from its subsidiary power company. These strengths are partially offset by the gloomy outlook for the printing industry, a short track record and the execution risks in the power segment, as well as a rising level of debt financing for the power-related investments.

EPCO was established in 1990 as a printing service provider. The company was listed on the Stock Exchange of Thailand (SET) in 1993. As of October 2017, Aqua Corporation PLC (AQUA) held approximately 38% of EPCO while the Chinsupakul family, the company's founders, owned 17%. EPCO provides a full range of printing services, serving both domestic customers and customers abroad. EPCO prints newspapers, magazines, product manuals, educational books, calendars, and advertising materials. EPCO has transitioned to focus heavily on the power business to make up for the drop-off in the printing business.

The rating recognizes EPCO's strong market position as a leading printing service provider due to its size and broad range of products. EPCO maintains long-term relationships with its customers on the strength of its long-established track record. However, the growth of digital media has tailed off industry-wide demand for printing services. As a result, EPCO's revenue from the printing segment has steadily declined to about Bt500 million annually over the past four years, compared with Bt600-Bt650 million annually during 2004-2012. Growth in printing revenue remains untenable over the long run.

That said, EPCO remains profitable and its gross margin is relatively higher than peers, backed by its robust customer base. On a stand-alone basis, EPCO's operating margin (operating profit before depreciation and amortization as a percentage of revenue) was over 10% for the past five years. In a bid to sustain its core business growth, EPCO plans to expand into packaging in anticipation of growing demand.

The rating also incorporates the company's advantageous diversification into the power industry. EPCO has diversified into the solar power business since 2012, primarily through its main subsidiary, Eastern Power Group PLC (EP). EPCO currently owns 75% of EP. EP launched two pilot solar farm projects in Kanchanaburi province in 2012. The contracted capacity of the two farms is 10 megawatts (MW). In 2013, the company added a 5-MW solar farm project in Lopburi province. During 2014-2015, the company developed eight solar rooftop projects in Bangkok and Samutprakan province, with a contracted aggregate capacity of 1.5 MW. All solar farm and rooftop projects are in operation. Each project obtains favorable tariffs according to multi-year power purchase agreements (PPAs) with the state-owned electricity distributors. During 2015-2016, EP acquired and developed a 9.9-MW solar farm project in Kyoto, Japan, at a cost of Bt1.03 billion. The project commenced operation in November 2016. EP also acquired a 5-MW co-operative solar farm project in Prachinburi province, at a cost of Bt268 million. The project commenced operation in December 2016.

In addition to its investment in solar power, EP recently invested Bt3.16 billion in two cogeneration power companies, a move that significantly increases its capacity and broadens the mix of energy that EP produces. EP purchased 49.5% of the shares of PPTC Co., Ltd. (PPTC) and 40% of SSUT Co., Ltd. (SSUT). PPTC's cogeneration power plant has been operational since March 2016. The plant has a capacity of 120 MW of electricity production and 30 tonnes of steam per hour. SSUT owns two plants with an aggregate capacity of 240 MW of power and 60 tonnes of steam per hour. SSUT achieved full operation in December 2016. The acquisitions will boost EPCO's earnings, as the cogeneration power plants combined add 155.4 megawatts equity (MWe) to EP's capacity (or capacity in proportion to EP's ownership of the respective power plants). In all, EP currently holds power projects with aggregate installed capacity of about 192 MWe.

The diversification to the power industry makes EPCO's cash flow more stable and, most importantly, helps ensure that earnings keep growing. EPCO's consolidated revenue in the first half of 2017 was Bt498 million, up 13% from one year ago. The operating margin in the first half of 2017 was 47.6%, increasing from 39.9% in 2016. EPCO's operating margin in the printing segment was stable, staying in a range of 18%-22% during 2014 through the first half of 2017.

EPCO's rating is, however, partially offset by the gloomy outlook for the printing industry, due for the most part to dwindling demand for printing services. The industry is at the precipice of a significant change due to competitive threats from digital media. The severity of the situation has crimped EPCO's core business growth. Although EPCO has strived to diversify, the short track record in the power segment keeps a lid on the rating. The rating is further weighed down by the execution risks in its current and forthcoming power projects. EPCO, through EP, invested heavily in cogeneration, which is more complicated and carries higher execution risks than solar power. In the first year of operation, PPTC has so far demonstrated a satisfactory performance while SSUT's plants still need to be fine-tuned.

The rating is also tempered by a rise in EPCO's debt level as it borrows more to fund the power-related investments. EPCO's investments in cogeneration power projects and a solar power project in Japan significantly raised its debt to capitalization ratio to 65% in 2016 and 70.2% as of June 2017, compared with 43.7% in 2015. The company plans to invest in more solar farm projects in Japan, adding 25 MW of new capacity. The total cost of the new projects abroad is Bt2.7-Bt3 billion, with construction planned for 2018-2019. Should the deals be executed, EPCO would shoulder a higher debt load during the development phase. In the near term, TRIS Rating does not expect huge investments apart from the 25-MW Japan-based solar farms unless EP is able to raise additional capital, in particular from an initial public offering (IPO).

TRIS Rating does not expect resurgence in the printing industry in the near term. Despite EPCO's effort to expand into packaging, revenue from the printing segment will remain tame. Going forward, the power segment will bring in about half of EPCO's total revenue but contribute a much larger portion of profit. TRIS Rating's base case assumes EPCO's revenues will be at least Bt950 million per annum during 2017-2020. Operating income is expected to grow as a result of a larger revenue base and more stable income from the power segment. The operating margin is expected to stay at around 45%. Funds from operations (FFO) are expected to total Bt500-Bt600 million per annum. TRIS Rating also expects EPCO to recognize a substantial share of profit on investment in the two cogeneration companies from 2018 onwards.

Looking ahead, the company is expected to keep the debt to equity ratio below 3 times. Cash flow protection, as measured by the FFO to total debt ratio and the ratio of earnings before interest, tax, depreciation, and amortization (EBITDA) interest coverage, weakened recently but is expected to gradually improve once the huge investments in the power segment come to fruition. However, these two ratios should remain consistent with the current rating. During 2017-2020, the FFO to total debt ratio is expected to stay around 12%-15%, while the EBITDA interest coverage ratio will remain at 3-5 times. The total debt to capitalization ratio is expected to stay in a range of 60%-70% over the next three years.

Rating Outlook

The "stable" outlook reflects the expectation that EPCO will maintain its strong market position in the printing segment and that this segment will remain profitable. In addition, EPCO will realize sizable and sustainable cash flows from the power segment. Further, EPCO is expected to successfully execute the power projects in Thailand and abroad, and earn satisfactory returns, without substantially deteriorating its capital structure.

A credit upside could develop as EPCO builds a track record in the power segment with a larger cash flow base, despite greater exposures to operational risks, while its debt to capitalization ratio declines and stays below 60%. Conversely, downward pressure on the rating could emerge should EPCO fail to maintain its strengths in its core business or fail to achieve recurring cash flow from the power segment. Each of these two unfavorable outcomes would lower EPCO's profitability and raise its leverage from the current level, plus cause the debt to capitalization ratio to exceed 70% for a sustained period.

Eastern Printing PLC (EPCO)

Company Rating:	BBB
Rating Outlook:	Stable

Financial Statistics and Key Financial Ratios*

Unit: Bt million

		---------------------Year Ended 31 December --------------------				
	Jan-Jun 2017	2016	2015	2014	2013	2012
Revenue	498	855	859	872	759	661
Gross interest expense	95	110	51	59	47	6
Net income from operations	132	119	233	218	131	66
Funds from operations (FFO)	164	226	331	325	245	112
Earnings before interest, tax, depreciation, and amortization (EBITDA)	318	365	398	396	299	142
Capital expenditures	184	1,074	77	232	400	819
Total assets	8,086	7,206	2,579	2,680	2,141	1,804
Total debts	5,516	4,527	1,071	1,184	1,138	887
Shareholders' equity	2,346	2,437	1,381	1,383	878	779
Operating income before depreciation and amortization as % of sales	47.6	39.9	44.4	42.9	36.2	16.9
Pretax return on permanent capital (%)	5.4**	5.6	11.8	13.1	12.0	7.9
Earnings before interest, tax, depreciation, and amortization (EBITDA) interest coverage (times)	3.3	3.3	7.9	6.7	6.3	22.4
FFO/total debt (%)	3.9**	5.0	30.9	27.4	21.5	12.6
Total debt/capitalization (%)	70.2	65.0	43.7	46.1	56.4	53.3

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

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