

EAST COAST FURNITECH PLC

No. 118/2021

30 July 2021

CORPORATES

Company Rating:	BB+
Outlook:	Stable

Last Review Date: 23/07/20

Company Rating History:

Date	Rating	Outlook/Alert
23/07/20	BB+	Negative
25/07/18	BB+	Stable
19/06/17	BB	Stable

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RATIONALE

TRIS Rating affirms the company rating on East Coast Furnitech PLC (ECF) at “BB+” and, at the same time, revises the rating outlook to “stable” from “negative”. The “stable” outlook reflects ECF’s rising furniture sales which benefit from the stay-at-home trend due to the Coronavirus Disease 2019 (COVID-19) pandemic and easing pressure of its financial leverage following the divestment of its biomass power plants.

The “BB+” rating continues to reflect ECF’s adequate competitive strength in the furniture market and established distribution channels through modern-trade retailers in Thailand and export. However, the rating is weighed down by its highly leveraged balance sheet and development risks associated with the “Minbu” project, a 220-megawatts (MW) solar power project in Myanmar.

KEY RATING CONSIDERATIONS

Adequate competitive strength in furniture market

ECF’s business profile is underpinned by its established market position as a medium-sized furniture manufacturer in Thailand. The company is considered an Original Equipment Manufacturer (OEM) since majority of its furniture sales are made-to-order products. We view ECF’s competitive strength as adequate to maintain its market position, backed by its own production facilities and economies of scale, compared with most furniture manufacturers.

Nevertheless, its business profile is constrained by price-driven competition in the furniture market as most products are simple knockdown furniture targeted at the low- to medium-priced segments.

Established distribution channels

ECF has two core distribution channels, comprising exports and Thai modern-trade retailers. Most of ECF’s export customers are leading furniture and modern trade retailers in Japan. The company has distributed through these two distribution channels for longstanding periods, and they have been an essential factor supporting sales growth for several years. In 2020, the made-to-order or export market accounted for 65% of ECF’s total furniture sales, and Thai modern trade made up about 29% of the total.

Stay-at-home trend bolsters revenue growth

ECF’s business has benefited from the booming demands for furniture, resulting in a quick rebound in ECF’s operating performance in the second half of 2020. For the whole of 2020, total revenue increased by 10% to THB 1.4 billion. The export channel displayed a material growth rate of 23% year-on-year (y-o-y). Meanwhile, the furniture sale through the Thai modern trade retailers increased by about 3.7% y-o-y.

A sharp rise in purchase orders from customers in the United States (US) and India is the main reason for revenue recovery. These new customers are online furniture retailers benefiting from stay-at-home and online shopping trends. Revenues from the US customers accelerated to THB103 million in 2020 and to THB40 million for the first three months in 2021 from THB14 million in 2019. The Indian market had also performed well, with soaring revenue to THB79 million in 2020, before dropping sharply in the first quarter of 2021, due to the impact of the severe COVID-19 outbreaks in the country.

Our base-case scenario assumes ECF's revenue to climb to a record high of THB1.6 billion in 2021 before decelerating during 2022-2023. The company resumed shipments to India in the second half of 2021 after the easing of COVID-19 situation in the country.

Rising production costs pulling down profitability

ECF's profitability has been under pressure from significantly rising production cost. The earnings before interest, taxes, depreciation and amortization (EBITDA) margin was curtailed to 13.7% in 2020 and 12.6% in the first quarter of 2021, compared with 17%-18% during 2017-2019. The margin has been squeezed by a spike in particleboard prices and higher labor cost during the COVID-19 pandemic. However, we expect its profitability to improve gradually, backed by an increase in the utilization rate of production capacity and the company's efforts to reduce raw material cost.

Lower-than-expected financial leverage

ECF's financial results for 2020 were better than our forecast. ECF's financial leverage currently remains at an endurable level. The improved operating results were attributed to the strong demands for furniture in the second half of 2020 and the company's success in divesting the investment in Safe Energy Holdings Co., Ltd. (SAFE), an operator of biomass power plants. The THB233 million proceeds of the divestment are used to fund the equity injection for the remaining phase of the Minbu project.

Financial profile expected to improve

We expect ECF's financial profile to improve after the remaining phases of the Minbu project commence operation. Phase 2-4 of the project have been delayed due to the COVID-19 outbreak and the political situation in Myanmar.

In our base-case forecast, we assume phase 2 of the Minbu project will commence operation in 2022 with the remaining phases in 2023, or about one year delay from previous plans. We expect the entire operation of Minbu's power plant will render ECF a steady cash flow of THB100-THB120 million per annum. We project ECF's EBITDA to increase to about THB300 million in 2023 from THB200 million in 2021, and its net debt to EBITDA ratio to decline to 5-7 times, and the fund from operation (FFO) to net debt ratio to increase to 5%-10% over the forecast period.

Tight liquidity

We assess that ECF's liquidity is still tight. The sources of funds are slightly higher than the uses of funds over the next 12 months. The sources of funds consist of cash on hand as of March 2021 at THB81 million and an estimated FFO of THB57 million. The uses of funds will be capital spending of THB61 million, loan repayment over 12 months of THB52 million, and dividend of THB12 million.

Capital structure

At the end of March 2021, ECF had THB1.85 billion in debt, including around THB1.47 billion of the priority debt. All priority debts are secured debts. This means the ratio of priority debt to total debt was about 79.5%. As its priority debt ratio is more than the threshold of 50%, we view that ECF's unsecured creditors are significantly disadvantaged with respect to the priority of claim against ECF's assets. As a result, the rating on the senior unsecured debt issue of ECF will be one notch lower than the company rating.

BASE-CASE ASSUMPTIONS

- Revenue to be around THB1.6 billion in 2021 and to grow by 1%-2% during 2022-2023.
- Shared profits from the Minbu investments to rise to THB100 million in 2023 from about THB30 million in 2021.
- EBITDA margin, including cash flow from the Minbu project, to grow to 19% in 2023 from 13% in 2021.
- Capital expenditure to be THB60 million per year during 2021-2023.
- Dividend payout ratio to be 30% during 2021-2023.

RATING OUTLOOK

The "stable" outlook reflects our expectations that the company's furniture business will continue to operate smoothly, and its financial leverage to improve once the Minbu project is in full operation.

RATING SENSITIVITIES

The prospect of a rating upgrade is limited in the near term due to the company's highly leveraged balance sheet. A rating downgrade could occur if ECF's financial position deteriorates further. This could result from weakening performance in the furniture business and/or additional debt-financed investments. The adverse changes in the Minbu project that has a

negative impact on ECF's cash flows may also trigger a negative rating action.

COMPANY OVERVIEW

ECF engages in the manufacture and distribution of home furniture in Thailand. The company owns two factories in Rayong province, focusing on producing knockdown furniture and rubber wood furniture. Revenue from selling furniture contributes over 90% of its total revenue; the remainder is derived from selling decorative foil paper and dried rubber wood. ECF has been listed on the Market for Alternative Investment (MAI) since 2013. The Suksawad family is the main shareholder, holding approximately 50% of the company's outstanding shares as of 30 June 2021.

ECF distributes its furniture products through two main channels, including made-to-order for export and Thai modern trade. Almost all made-to-order furniture is exported to leading furnishing distributors and large modern trade retailers in Japan. In Thailand, the company distributes furniture through well-known modern trade retailers, such as Home Pro, Big C, Mega Home, Thai Wasadu, Tesco Lotus, and Global House.

The company, through ECF Power Co., Ltd., has invested in the Minbu project, a 220-MW solar power plant in Myanmar. The project consists of four phases. The first phase with 50 MW already achieved the commercial operating date in September 2019.

KEY OPERATING PERFORMANCE

Table 1: ECF's Power Project Portfolio as of 30 Jun 2021

Project/Country	Type	Hold by ECF (%)	Installed Capacity (MW)	Contracted Capacity (MW)	COD
Myanmar					
Minbu project					
- Phase 1	Solar	20	50	40	Sep 2019
- Phase 2	Solar	20	50	40	2022
- Phase 3	Solar	20	50	40	2023
- Phase 4	Solar	20	70	50	2023
Total			220	170	

Source: ECF

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS*

Unit: Mil. THB

	Jan-Mar 2021	----- Year Ended 31 December -----			
		2020	2019	2018	2017
Total operating revenues	409	1,401	1,273	1,442	1,479
Earnings before interest and taxes (EBIT)	49	172	186	145	157
Earnings before interest, taxes, depreciation, and amortization (EBITDA)	52	192	228	246	253
Funds from operations (FFO)	17	45	103	129	160
Adjusted interest expense	35	133	118	104	81
Capital expenditures	14	100	57	136	33
Inventory	3,544	3,545	3,348	3,396	2,780
Total assets	1,369	1,370	1,379	1,172	999
Adjusted debt	1,767	1,684	1,608	1,299	1,176
Adjusted equity	1,271	1,240	1,242	1,447	1,027
Adjusted Ratios					
EBITDA margin (%)	12.6	13.7	17.9	17.0	17.1
Pretax return on permanent capital (%)	5.6 **	5.5	6.2	5.4	7.1
EBITDA interest coverage (times)	1.5	1.4	1.9	2.4	3.1
Debt to EBITDA (times)	8.7 **	8.8	7.0	5.3	4.6
FFO to debt (%)	3.1 **	2.7	6.4	9.9	13.6
Debt to capitalization (%)	58.2	57.6	56.4	47.3	53.4

* Consolidated financial statements

** Annualized with the trailing 12 months

RELATED CRITERIA

- Rating Methodology – Corporate, 26 July 2019
- Key Financial Ratios and Adjustments, 5 September 2018

East Coast Furnitech PLC (ECF)

Company Rating:

BB+

Rating Outlook:Stable

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