TRIS RATING
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ESSO (THAILAND) PLC

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CORPORATES

Company Rating: A
Outlook: Stable

Last Review Date: 11/06/20

Company Rating History:

Date	Rating	Outlook/Alert
11/06/20	A	Stable
21/11/08	A+	Stable

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RATIONALE

TRIS Rating affirms the company rating on Esso (Thailand) PLC (ESSO) at "A" with a "stable" outlook. The rating reflects ESSO's strong tie with Exxon Mobil Corporation and affiliates (ExxonMobil Group), its efficient integrated refinery, and strong market presence. Conversely, the rating is constrained by the high volatility of the petroleum and petrochemical industries, and intense competition in the retail business. The rating also reflects the uncertain prospects of a revival of the refining industry.

KEY RATING CONSIDERATIONS

Severe impacts from oil market turmoil

The fierce price war together with the unprecedented COVID-19 pandemic have had severe repercussions on the global supply and demand for oil. The impact of the turmoil in the oil markets on ESSO is reflected in the company's substantial loss for the first nine months of 2020 due to hefty inventory losses and a sharp compression in gross refinery margin (GRM).

The COVID-19 pandemic starting in late first quarter 2020 and a fierce price war between influential global oil suppliers, resulted in the Dubai crude oil price plunging to USD21 per barrel in April 2020, from USD64 per barrel in January 2020. The immediate impact on most oil refiners was a huge inventory loss. Although the oil price gradually recovered to a level of USD40-USD45 per barrel in the third quarter of 2020, it was not enough to offset the inventory loss incurred in the first half of the year.

Weakening oil demand, especially in the ailing aviation sector, sent refining margins tumbling to their lowest levels in years. Jet fuel consumption has endured the biggest impact from the pandemic. In response, many refiners are attempting to minimize jet fuel output by switching to diesel fuel production instead. ESSO's total GRM (market GRM plus gain and loss in inventory) steeply declined to negative USD6.7 per barrel for the first nine months of 2020, compared with a positive USD3.0 per barrel for the same period of 2019.

The tumbling demand led to a drastic reduction in ESSO's production. The company's crude run was 114 thousand barrels per day (KBD), suggesting a 66% capacity utilization rate. As a result, ESSO recorded a net loss of THB8.3 billion and negative earnings before interest, tax, depreciation, and amortization (EBITDA) of THB8.2 billion for the first nine months of 2020.

A part of ExxonMobil Group

The rating affirmation takes into consideration ESSO's status as the local arm of the ExxonMobil Group, a leading global refiner and distributor of petroleum products. The rating is in part reflective of the ongoing supports ESSO receives from the ExxonMobil Group, as well as our view of a high likelihood of financial support from the ExxonMobil Group in a stress scenario.

Operationally, ESSO leverages ExxonMobil Group's global supply chain in procuring crude oil and other feedstocks. The company also sells its refined petroleum and petrochemical products through the group's distribution network. The company adopts ExxonMobil Group's technology and maintains group standards in its refinery and petrochemical plant operations.

Added to that, ESSO is entitled to access and adopt technology and management practices developed by the ExxonMobil Group, through various agreements with the group. More importantly, ESSO receives financial support from the ExxonMobil Group from time to time, which helps enhance its financial flexibility.

Flexible refining facility

ESSO's refinery is ranked in the top tier of energy-efficient plants in the Asia-Pacific region, with high operational reliability. The company's complex refinery is integrated with an aromatics plant, which enables ESSO to adjust its crude slate and product mix.

ESSO has shown its operating flexibility by adjusting its product mix in response to the drop-off in demand for jet fuel. ESSO has converted most of its jet fuel production to diesel production. For the first nine months of 2020, ESSO's refinery product mix was diesel (41%), gasoline (20%), feedstocks for chemicals products (18%), jet fuel and kerosene (3%), fuel oil (8%), and others (10%). The proportion of Jet fuel dropped dramatically from 9% of total production in 2019.

Strong market presence

ESSO has a strong market presence in Thailand, led by its extensive distribution network of service stations operated under the "ESSO" brand. Over the past three years, ESSO has focused on expanding its distribution network as well as renovating its service stations and offering new premium products to the market. The number of service stations has rapidly increased from about 500-550 during 2012-2017 to 676 stations as of September 2020.

Given its strong brand, ESSO is well positioned to market its premium oil and related products through its service stations. The company's service stations are capable of generating a relatively high volume of sales per station compared with most of its peers. The company has also focused more on the non-oil business to support the growth of its fuel retailing business, a strategy used to gain more profit from the retail business while alleviating the volatile effects of its refining business.

Intense competition in the retail business

The company's efforts to strengthen its retail business have faced tough challenges as most oil retailers in the Thai market are continuing to expand their service stations networks and launching promotional campaigns to gain market share. In addition, retailers have spent heavily to renovate their petrol stations and have begun offering non-oil goods and services. The petrol stations makeover is a trend seen industry wide.

The COVID-19 outbreak caused domestic petroleum consumption to plunge by about 25% year-on-year (y-o-y) in April-May 2020, the period of peak pandemic fear. As for the retail market, total sales through service stations tumbled by 20% y-o-y in April 2020. However, the retail segment has recovered substantially since the easing of the virus containment measures. Domestic demand for transportation fuel is almost back to the pre-COVID level.

Operating performance expected to gradually improve

Looking forward, we expect ESSO's operating performance will gradually improve, assuming no further huge inventory losses during the forecast period. Our forecast is built on our expectation of a resurgence in oil prices and crack spreads (the difference between refined product price and crude oil price). That said, we view that the lingering effect of the pandemic will continue to depress fuel demand and muddy the outlook of the refining industry. Although the development of vaccines holds out hopes for a recovery, we do not expect a quick turnaround of GRM to pre-pandemic levels.

We forecast the crude price to average about USD40 per barrel in 2020, increasing to USD45 per barrel in 2021 and USD50 per barrel in 2022-2023. The crack spread might take 1-2 years to recover to the normal level. In our base-case forecast, we project ESSO to incur negative EBITDA of about THB6.5-THB7.5 billion in 2020, reflecting a softening GRM. ESSO's refinery remains under immense pressure, given the thin crack spreads for most refined products.

We project the company's debt to capitalization ratio will be around 70% at the end of 2020 and expect its EBITDA to turn positive in the range of THB4.0-THB5.0 billion per year during 2021-2023. The debt to EBITDA ratio is expected to stay over 6 times, and the debt to capitalization ratio in the 60%-70% range during 2021-2023.

Satisfactory liquidity profile

We believe ESSO has sufficient sources of liquidity to manage its debts coming due in the next 12 months. As of September 2020, ESSO had cash on hand of about THB350 million and undrawn credit facilities from commercial banks of about THB18.9 billion, as well as a back-up credit facility from the ExxonMobil Group of THB54 billion. The company is obliged to repay long-term bank loans of THB2.0 billion over the next 12 months.

Financial support enhances ESSO's financial flexibility

Given its strong link with the ExxonMobil Group, we believe ESSO will continue to receive financial support from the ExxonMobil Group. This is evidenced by the credit lines ESSO has received in the past years. As of September 2020, about two-thirds of ESSO's total debt was owed to the ExxonMobil Group. On top of the outstanding inter-company debt, the ExxonMobil Group has provided a credit facility of THB54 billion to ESSO, which currently remains undrawn.

BASE-CASE ASSUMPTIONS

- Dubai crude oil price to average about USD40 per barrel in 2020, USD45 per barrel in 2021 and USD50 per barrel in 2022-2023
- GRM to range from USD3-USD4 per barrel during 2021-2023
- ESSO's crude run to be in the range of 125-135 thousand barrels per day (KBD) during 2021-2023
- Capital expenditure forecast at about THB1.5 billion per year during 2021-2023

RATING OUTLOOK

The "stable" outlook takes into account the strong link between ESSO and the ExxonMobil Group, and our expectation of continued support from the ExxonMobil Group. We also expect the company to maintain its sound market presence in the petroleum business in Thailand, with improved performance over the next few years against a backdrop of gradual recovery in its refining business.

RATING SENSITIVITIES

ESSO's credit upside is limited over the next 12-18 months but it could occur if ESSO stages a quick turnaround, with significant improvement in profitability and lower financial leverage. In contrast, the rating could come under pressure if ESSO's operating performance turns out to be significantly worse than our expectation, or there is a material adverse change in the on-going support received from the ExxonMobil Group.

COMPANY OVERVIEW

ESSO is the Thailand-based affiliate of Exxon Mobil Corporation (ExxonMobil), which is one of the world's largest oil refiners and petrochemical companies. ESSO has a long track record in the petroleum business in Thailand. The company and its affiliates began the oil business in Thailand in 1894 and opened a refinery in 1971. As of June 2020, ESSO's major shareholders comprised ExxonMobil Asia Holding Pte. Ltd. (65.99%) and Vayupak Fund 1 (9.7%).

ESSO operates a complex refinery with a maximum rated capacity of 174 KBD, accounting for approximately 14% of the total refinery capacity in Thailand. ESSO also operates an aromatics plant, which is integrated with the refinery. The aromatics plant has a production capacity of 500 thousand tonnes per annum of paraxylene. In addition, there were 676 service stations operating under the "Esso" brand name, as of September 2020.

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS*

Unit: Mil. THB

			-------------Year Ended 31 December	----------		
	Jan-Sep 2020		2019	2018	2017	2016
Total operating revenues	94,254		169,430	200,864	178,839	151,102
Earnings before interest and taxes (EBIT)	(10,238)		(3,403)	3,105	9,553	8,881
Earnings before interest, taxes, depreciation, and amortization (EBITDA)	(8,174)		(1,315)	5,158	11,570	11,153
Funds from operations (FFO)	(6,280)		(977)	4,279	9,306	8,922
Adjusted interest expense	269		554	450	562	675
Capital expenditures	1,257		1,659	1,345	1,161	1,446
Total assets	59,302		66,243	61,750	59,020	58,751
Adjusted debt	35,984		32,405	19,779	16,650	26,540
Adjusted equity	13,432		22,118	25,832	28,182	20,752
Adjusted Ratios						
EBITDA margin (%)	(8.67)		(0.78)	2.57	6.47	7.38
Pretax return on permanent capital (%)	(25.21)	**	(6.75)	6.80	20.51	18.76
EBITDA interest coverage (times)	(30.39)		(2.37)	11.47	20.58	16.52
Debt to EBITDA (times)	(3.66)	**	(24.64)	3.83	1.44	2.38
FFO to debt (%)	(21.42)	**	(3.01)	21.64	55.89	33.62
Debt to capitalization (%)	72.82		59.43	43.36	37.14	56.12

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

RELATED CRITERIA

- Rating Methodology – Corporate, 26 July 2019
- Key Financial Ratios and Adjustments, 5 September 2018
- Group Rating Methodology, 10 July 2015

Esso (Thailand) PLC (ESSO)

Company Rating:	A
Rating Outlook:	Stable

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