TRIS RATING
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THAI POLYCONS PLC

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CORPORATES

Company Rating:	BBB-
Outlook:	Negative

Last Review Date: 28/10/22

Company Rating History:

Date	Rating	Outlook/Alert
29/10/21	BBB-	Stable
09/10/18	BBB	Stable

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RATIONALE

TRIS Rating affirms the company rating on Thai Polycons PLC (TPOLY) at "BBB-". However, we revise the rating outlook to "negative" from "stable" to mirror a slower-than-expected earnings recovery, particularly in its construction business. The outlook revision also reflects our view that the company's earnings revival remains fragile due to several uncertainties.

The rating continues to reflect the reliable cash generation from TPOLY's power business, which has considerably helped offset repercussions from the cyclical nature of its construction business. However, the strengths of the power business are held back by susceptibility to a feedstock supply risk and volatile prices, the increasingly competitive renewable power industry, and the risks associated with the company's first overseas power project. Also, the rating remains constrained by the company's mediocre competitive position in the construction business, resulting in consistently thin profit margins.

KEY RATING CONSIDERATIONS

Recovery slower than expected

TPOLY's overall performance remains greatly influenced by the construction business. Although the power business has been the company's profit center, the construction business has represented about half of its revenue. The construction business has delivered very thin margins over the past several years.

TPOLY's operating performance has recently improved after the pandemic. Its earnings before interest, taxes, depreciation, and amortization (EBITDA) rose to THB511 million during the first half of 2023, from THB248 million during the same period last year. That said, TPOLY's earnings are recovering at a slow pace, compared with the expectation in our previous assessment. The profit contribution came solely from the power business. The construction business could strive towards a recovery, but its operations remained weak and incurred operating loss.

Based on recent operating results, we slash our estimate on the gross margin of the construction business to 1% in 2023, as opposed to nearly 4% in our previous forecast. The gross margin of the construction business is assumed to improve gradually to 5%-7% in 2024-2025. Inclusive of the lucrative power business, TPOLY's overall gross margin should be about 14% in 2023 and increase to 19%-20% during 2024-2025.

Although we expect TPOLY to remain on a recovery path, we view the performance revival as fragile due to strong headwinds, such as escalating costs, interest rate hikes, highly competitive market, and repeated delays in the bidding and awarding of new construction projects.

Mediocre competitiveness in construction business

We continue to assess TPOLY's competitiveness in the construction business as mediocre, considering its business scale and track record. Most of the company's construction work is worth below THB1 billion per contract, resulting in a small revenue base of about THB2 billion per annum. TPOLY also engages in a narrow scope of construction work, focusing on the construction of buildings, such as hospitals, universities, hotels, and shopping malls.

Slowdown in growth of the domestic economy has led to intensified competition. This will constrain the amounts of new construction contracts and profit margins. TPOLY acquired new construction contracts worth a mere THB330 million in total during the first nine months of 2023, compared with THB1-THB3 billion per annum in the recent past. TPOLY's construction backlog stood at THB1.9 billion as of June 2023. We expect the company to acquire more construction contracts to replenish the backlog.

Reliable cash flows from power business

TPOLY's rating mainly stems from the reliable cash flows from its power business, which represent more than 90% of its EBITDA. The power business is carried out by its core and profit-making subsidiary, TPC Power Holding PLC (TPCH). Currently, TPCH owns 14 power projects comprising biomass power, waste-to-energy (WTE), and a recently acquired solar power project. In all, TPCH's contracted capacity is 212.2 megawatts (MW).

The reliable cash flows from the power business are underpinned by multi-year power purchase agreements (PPAs) with credible state-owned producers and distributors of electricity. The earnings from the power business are crucial in our assessment of TPOLY's credit profile, helping counteract the weak earnings of the construction business.

Susceptibility to feedstock risk

The power business is highly susceptible to feedstock supply risk. The biomass power plants use woodchip, rice husk, coconut shells, and other fast-growing plants to produce electricity. The availability of feedstock relies on several factors, such as seasonality, use of biomass in other industries, and number of biomass power plants. To ensure availability of feedstock, the power business operator, TPCH, has secured long-term supply agreements with local suppliers. However, contract enforcement remains challenging.

Also, earnings of power plants are exposed to the volatile prices of feedstock. Biomass fuel prices can swing wildly while feedstock varies in terms of humidity and calorific value. As for WTE, different types of waste provide different calorific value, while contaminants can affect operational stability.

Intensified competition in power market

We view the increasingly intensified competition as putting significant downward pressure on earnings, notwithstanding growth opportunities for the renewable power industry in Thailand. The prospects of high-profit projects look limited. TPCH's most recent biomass power plants (TPCH1, TPCH2, and TPCH5) receive significant lower tariff rates, due to highly competitive bidding. The lower incentives cut the rates of returns on new projects, forcing TPCH to shift towards investing in other types of renewable power such as WTE and solar power. Also, TPCH is looking for growth outside Thailand with an eye on neighboring countries.

TPCH plans to divest a pool of five biomass power projects (TPCH1, TPCH2, TPCH5, PBM, and PBB), with a combined contracted capacity of 30.4 MW. In our base case, we assume the divestment to be completed in the last quarter of 2023 and TPCH to earn about THB1.2 billion in proceeds.

Overseas investment risks

TPCH has recently expanded outside Thailand, with its first overseas power project in the Lao People's Democratic Republic (Lao PDR). TPCH has recently acquired a 40% stake in Maekhong Power Co., Ltd. (MKP) worth about THB430 million. Incorporated in the Lao PDR, MKP is developing a 100-MW solar farm project, which carries a 25-year PPA with Electricite du Laos (EDL). The project is slated to start commercial run in 2024, receiving a fixed tariff rate over the PPA life.

The project is part of the PPA between EDL and Electricity of Cambodia (EDC). EDL will procure electricity from several sources, including the solar farm, and sell to EDC. This implies that EDC should be an indirect off-taker of the project. As a result, the market risk is somewhat mitigated. Nevertheless, the counterparty of MKP is still EDL.

We view TPCH's first overseas project as carrying higher country and regulatory risks relative to Thailand-based power generation assets. The credit profile of the state-run EDL, the purchaser of electricity, is not as strong as the state-owned power buyers in Thailand. The weakened credit profile of EDL increases the counterparty risk to TPCH. Also, TPCH will be exposed to the cross-border risks of fund transferability and currency convertibility in relation to the dividend income TPCH will receive from MKP. Additionally, the solar power project offers a challenging tariff rate of US$6.2 cents per kilowatt-hour (kWh). MKP has entered into an operating and maintenance agreement on agreed prices to control operating costs. With TPCH increasingly seeking more opportunities in neighboring countries, we expect TPCH's new investments to arrive at returns commensurate with their respective risks.

Revenue to decline, earnings to improve

TPCH, as a project sponsor, has provided guarantees on the debts of the incorporated joint ventures (JVs) in proportion to its stakes in the JVs. In assessing TPOLY's financial profile and performance, we consolidate the assets, liabilities, and respective financial performances of such JVs in TPOLY's consolidated accounts, in proportion to the ownership of TPCH in each venture.

We expect a plan to divest the existing 30.4-MW biomass power projects to lower TPOLY's total operating revenue to THB4.5-THB5 billion per annum during 2024-2025, from THB6.4 billion in 2023. In our base-case projection, we assume the remaining biomass power plants will continue to deliver satisfactory performance. Revenue from the power business should fall to THB2.5-THB2.7 billion per annum during 2024-2025, from THB3 billion in 2023. The divestiture will likely help increase profitability as the five biomass power projects to be sold carry low tariff rates and have low efficiency, relative to the other existing power projects.

Revenue from the construction business is forecast to stay in the THB2-THB3.3 billion per annum range during 2023-2025, given our assumption that TPOLY will secure new construction contracts worth THB1-THB2 billion annually. We expect TPOLY's profit margins to gradually increase, with more concise budgeting and cost controlling.

Taking these into account, we forecast TPOLY's EBITDA to range from THB0.9-THB1 billion per annum during 2023-2025, up from THB0.6 billion in 2022. Despite the increase, the level of EBITDA remains lower than our previous estimate of about THB1.1 billion annually. Our base-case projection assumes the company's EBITDA margin to stay in the 15%-20% range over the next three years.

Financial leverage to decline

The plan to sell off five biomass power projects should bring in THB1.2 billion in cash. With that, we assume TPOLY will invest in a green-field power project worth below THB 1 billion. Meanwhile, we assume TPCH's JVs will secure a new 10-MW WTE project. We also assume MKP could seek project loans, without the requirements of guarantees or additional financial supports by the sponsor over the course of the solar project development. We do not expect any material investments in the construction business.

Alongside performance recovery, the company's debt to EBITDA ratio will likely fall to 6.5-7.5 times during 2023-2025, from 8.7 times (annualized with trailing 12 months) in the first half of 2023. The ratio of funds from operations (FFO) to debt is projected to improve to 8%-10% and the debt to capitalization ratio should hover around 65% over the next three years. Capital spending will total about THB2 billion over the forecast period. TPOLY should also manage its working capital for the construction business efficiently to avoid a rise in financial leverage. Despite the expectation of lowering financial leverage and reviving earnings, the "negative" outlook incorporates the fact that our forecast remains susceptible to the lingering downside risks of the construction business.

Debt structure

In assessing the level of priority debt in TPOLY's borrowings, we exclude the debt incurred by the JVs which is guaranteed by TPCH. As such, TPOLY's consolidated debt was about THB7 billion as of June 2023. Of this, about THB6 billion was considered priority debt, comprising TPOLY's secured debt and all borrowings incurred by its subsidiaries. The priority debt to total debt ratio was 85%, suggesting that the company's unsecured creditors are significantly disadvantaged to its priority debt holders with respect to claims against the company's assets.

Rollover risk

Excluding the JV's debt, TPOLY had short- and long-term loans coming due in the next 12 months of about THB3.3 billion in total as of June 2023. This included debentures worth THB1.5 billion maturing in June 2024. We expect short-term loans for working capital to be rolled over as usual. At the same time, long-term project loans should be covered by cash flows from the respective operating power projects. TPOLY plans to repay the debentures with the proceeds from project refinancing. Other sources of cash are estimated to be THB1.1 billion in aggregate, which includes the expected FFO of about THB550 million and available undrawn credit facilities, plus cash and marketable securities, of THB582 million. The proceeds from asset sales will also help support liquidity. Given its growth plan, we view TPOLY as needing to refinance the debentures coming due with a new debenture issuance.

TPOLY's debenture obligations require the company to maintain an interest-bearing debt to equity ratio below 2.5 times. The ratio stood at 1.9 times as of June 2023. Also, the company's subsidiaries, including TPCH and its subsidiaries, as well as JVs, are required to meet the financial covenants set forth under their respective loan obligations. We expect all of them to be compliant with such requirements.

BASE-CASE ASSUMPTIONS

Key assumptions in TRIS Rating's base-case forecast during 2023-2025 are as follows:

- Aggregate contracted capacity of operating power plants to be 192 MW after project divestment.
- Average capacity factor of operating power plants to range between 80%-90%.
- New contracts for construction work to be worth THB1-THB2 billion annually.
- EBITDA margin to stay in 15%-20% range.
- Capital spending to total THB2 billion.

RATING OUTLOOK

The "negative" outlook reflects TPOLY's earnings recovering slower than we expected, due mainly to the weak performance of the construction business. The company's earnings revival remains fragile due to several uncertainties.

RATING SENSITIVITIES

We could downgrade the rating on TPOLY if its operating and financial results continue to be weaker than our estimates. Deterioration in its capital structure due to aggressive debt-funded investments may also lead to a rating downgrade. Conversely, the rating outlook could be revised to "stable" if TPOLY significantly improves its operating performance and lowers financial leverage. Also, we expect the power business to remain the core cash generator and continue to deliver satisfactory results. Investments in power projects that carry higher country risks should render commensurate returns.

COMPANY OVERVIEW

Established in 1988, TPOLY is a construction contractor providing engineering and construction (E&C) services to the public and private sectors. The company focuses on constructing buildings and civil works. The company was listed on the Market for Alternative Investment (MAI) in 2009 before switching to the Stock Exchange of Thailand (SET) in 2010. TPOLY expanded into the residential property and the power businesses in 2010. It spun off the power business to TPCH, its subsidiary, in 2012. The Chanpalangsri family remained the major shareholder, holding an approximate 42% interest in TPOLY, as of March 2023.

The construction business made up about half of TPOLY's total revenue. However, the power business accounted for the majority of TPOLY's earnings. EBITDA of the power business has made up more than 90% of TPOLY's EBITDA during the past three years. As of September 2023, TPOLY's power portfolio had an aggregate contracted capacity of 212.2 MW, across 12 biomass power projects (104.2 MW), one WTE project (8 MW), and one solar power project (100 MW). Thirteen of its power plants are currently operating (112.2 MW).

KEY OPERATING PERFORMANCE

Table 1: Revenue Breakdown

Unit: %

Segment	2019	2020	2021	2022	Jan-Jun 2023
Construction	55	55	43	47	57
Property	1	1	0	0	0
Power	43	45	57	53	42
Trading	0	0	0	0	0
Total	**100**	**100**	**100**	**100**	**100**
Total revenue (mil. THB)	**3,798**	**3,974**	**4,344**	**5,029**	**3,414**

Source: TPOLY

Table 2: Power Project Portfolio (as of Sep 2023)

Company/Country	Held by TPCH (%)	Status	Installed Capacity (MW)	Contracted Capacity (MW)	Tariff
Biomass Projects					
CRB	73	Operating	9.5	9.2	FiT
MWE	85	Operating	9.0	8.0	FiT
MGP	46	Operating	9.5	8.0	FiT
TSG	65	Operating	9.5	9.2	FiT
PGP	60	Operating	9.9	9.2	FiT
SGP	51	Operating	9.9	9.2	FiT
PTG	95	Operating	23.0	21.0	Adder
TPCH1	99	Operating	9.9	9.2	FiT
TPCH2	99	Operating	9.9	9.2	FiT
TPCH5	99	Operating	6.3	6.3	FiT
PBM	59	Operating	3.0	2.9	FiT
PBB	59	Operating	3.0	2.9	FiT
Sub total - Biomass			**112.4**	**104.2**	
Waste Projects					
SP	50	Operating	9.5	8.0	FiT
Sub total - Waste			**9.5**	**8.0**	
Solar Projects					
MKP	40	Developing	130.0	100.0	Fixed Rate
Sub total - Solar			**130.0**	**100.0**	
Grand total			**251.9**	**212.2**	

Source: TPCH

CRB	=	*Chang Raek Bio Power*	*MWE*	=	*Maewong Energy*
MGP	=	*Mahachai Green Power*	*TSG*	=	*Thungsung Green*
PGP	=	*Phathalung Green Power*	*SGP*	=	*Satun Green Power*
PTG	=	*Pattani Green*	*TPCH1*	=	*TPCH Power 1*
TPCH2	=	*TPCH Power 2*	*TPCH5*	=	*TPCH Power 5*
PBM	=	*Pracharat Biomass Mae Lan*	*PBB*	=	*Pracharat Biomass Bannang Sata*
SP	=	*Siam Power*	*MKP*	=	*Maekhong Power*

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS*

Unit: Mil. THB

	Jan-Jun 2023	------------Year Ended 31 December --------- 2022	2021	2020	2019
Total operating revenues	3,548	5,312	4,391	3,906	3,827
Earnings before interest and taxes (EBIT)	273	217	95	448	606
Earnings before interest, taxes, depreciation, and amortization (EBITDA)	511	602	481	704	797
Funds from operations (FFO)	319	289	275	581	667
Adjusted interest expense	186	296	194	123	102
Capital expenditures	124	423	504	1,428	1,704
Total assets	13,228	12,577	11,997	10,903	9,981
Adjusted debt	7,505	6,955	5,676	4,673	3,834
Adjusted equity	3,551	3,669	3,803	4,448	4,197
Adjusted Ratios					
EBITDA margin (%)	14.40	11.33	10.96	18.03	20.83
Pretax return on permanent capital (%)	3.89 **	2.03	0.97	5.05	8.26
EBITDA interest coverage (times)	2.75	2.03	2.48	5.73	7.85
Debt to EBITDA (times)	8.68 **	11.56	11.80	6.64	4.81
FFO to debt (%)	6.80 **	4.16	4.85	12.44	17.41
Debt to capitalization (%)	67.88	65.46	59.88	51.24	47.74

Note: The figures include assets, liabilities, and the respective financial performances of Mahachai Green Power Co., Ltd. (MGP) and Siam Power Co., Ltd. (SP), in proportion to the ownership stake in these JVs.

* *Consolidated financial statements*

** *Adjusted with trailing 12 months*

RELATED CRITERIA

- Group Rating Methodology, 7 September 2022
- Corporate Rating Methodology, 15 July 2022
- Key Financial Ratios and Adjustments for Corporate Issuers, 11 January 2022
- Issue Rating Criteria, 15 June 2021

Thai Polycons PLC (TPOLY)

Company Rating:	BBB-
Rating Outlook:	Negative

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