UNIQUE ENGINEERING AND CONSTRUCTION PLC

No. 47/2021
1 April 2021

CORPORATES

Company Rating:	BBB+
Issue Rating:	
Senior unsecured	BBB
Outlook:	Negative

Last Review Date: 30/04/20

Company Rating History:

Date	Rating	Outlook/Alert
25/06/18	BBB+	Stable

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RATIONALE

TRIS Rating affirms the company rating on Unique Engineering and Construction PLC (UNIQ) at "BBB+" and the ratings on UNIQ's senior unsecured debentures at "BBB". The issue ratings' one-notch below the company rating reflects UNIQ's high proportion of secured debts which have priority of claims against the company's assets compared to its unsecured borrowings. At the same time, TRIS Rating revises the rating outlook to "negative" from "stable". The revised outlook reflects the tendency of UNIQ's weakening earnings and increasing debt loads.

The ratings continue to reflect UNIQ's competitive strengths and sound profitability. However, these strengths are partially tempered by the company's high business concentration of construction projects in backlog. The ratings also recognize the fierce competition in the engineering and construction (E&C) industry and potential delays in the biddings of public construction projects, which could work to impede the revival of UNIQ's operating performance.

KEY RATING CONSIDERATIONS

Leading construction contractor

UNIQ's competitive strengths are underpinned by its track record of undertaking large-scale public infrastructure projects, including the Bang Sue-Rangsit section of the Red Line, the extension of the Green Line, and the Orange Line (Thailand Cultural Center-Min Buri). The company also owns facilities producing key building materials, such as precast yards and steel fabrication factories. UNIQ's earnings before interest, tax, depreciation, and amortization (EBITDA) were THB2.3-THB2.8 billion per year over the past five years.

UNIQ has ascended to become the fourth-largest E&C contractor listed on the Stock Exchange of Thailand (SET), as measured by revenue and asset size. UNIQ has focused on medium-to-large public infrastructure projects. Given its bidding qualification, UNIQ aims to tender a number of upcoming public projects, including the extension of the MRT Purple Line, the Thailand-China high-speed railway, inner-city motorways, and dual track railways.

Superior cost management

UNIQ had consistently attained sound profitability, with an EBITDA margin (EBITDA as a percentage of total operating revenues) of 19%-22% over the past five years, higher than other top-tier contractors. UNIQ's superior profitability has resulted from its centralized cost management that keeps track of changes in raw material purchases and prices, as well as increases its bargaining power with its suppliers. It also keeps the cost structure flexible by using a large number of sub-contractors. This strategy keeps overhead costs low as it can wind down or expand throughout the industry cycles by adjusting the amount of sub-contracted work. On the downside, this strategy could cause a shortage of workers. We expect the company to maintain its efficient cost controls amidst compressing gross margins.

High concentration in backlog

UNIQ's strengths are held back by its high business concentration. The company's backlog is dominated by a few large infrastructure projects. The three largest projects under construction make up about 80% of its backlog. Failure to complete one or more projects or any significant interruption in a project could have a material impact on operating performance.

Weakening earnings

The "negative" outlook embeds our expectation that UNIQ's earnings will remain under immense pressure, given its depleting backlog. UNIQ barely secured new contracts over the past three years, due mainly to delays in the biddings of public projects. As a result, its backlog fell steadily to THB12.5 billion in 2020, from a peak of about THB40 billion in 2017. Based on the current backlog, we expect UNIQ will continue to see earnings weaken in 2021. We forecast UNIQ's revenue will fall to THB8.3 billion in 2021, the lowest level seen in recent years.

In addition, we expect UNIQ's profitability to remain susceptible to fiercely competitive biddings, difficulties in raw material and workforce management during the Coronavirus Disease 2019 (COVID-19) pandemic, and delays of work schedules in some projects. Its gross margin declined to 18% in 2020, as opposed to around 20% three years earlier. We forecast its gross margin to stay below 20% over the next three years, with a significant fall in EBITDA to THB1.7 billion in 2021.

Rising debt loads and interest burden

UNIQ's financial profile has deteriorated significantly. UNIQ has undertaken large-scale public infrastructure projects, which are often faced with circumstances that lead to delays in project completion, such as delayed handovers of construction sites, revisions of project master plans, remedial work, and so on. A significant rise in working capital to support larger construction work pushed its adjusted debt to THB14.8 billion in 2020, up from THB10.7 billion a year earlier. UNIQ had a large sum of unbilled receivables, largely with respect to the double-track railways and the fourth contract of the Orange Line electric rail route. The company also had large amounts of outstanding account receivables related to the Red Line electric railway.

As the outstanding receivables are related to public projects, we view the payment risk as low. However, lengthy collection periods have weighed financially on UNIQ. The company's debt to EBITDA ratio surged to 6.5 times in 2020, up from 2-4 times in the recent past. With an expected decline in earnings, the debt to EBITDA ratio should stay over 6 times in 2021. Given the rising interest burden, we forecast UNIQ's funds from operations (FFO) will total THB980 million in 2021, a continued decline from recent years. The FFO to debt ratio will likely decline to about 9% in 2021.

Uncertainties impeding the recovery

We maintain a positive view on the domestic E&C industry over the medium term and believe UNIQ will be well positioned to capitalize opportunities from the government's fiscal stimulus measures that center on launching new infrastructure projects. Hence, we expect UNIQ's earnings will likely recover in the years ahead.

Our base-case forecast assumes UNIQ will secure new construction contracts of THB5-THB20 billion per year over the next 3 years, boosting total operating revenue to THB11-THB12 billion in 2022-2023. We expect UNIQ's gross margin to bottom at about 14% in 2021. The gross margin should recover to 18% when revenue bounces back during 2022-2023. We believe UNIQ will put much effort into cutting operating costs to alleviate the impact of compressing gross margins. We expect UNIQ's EBITDA to improve to about THB2.5 billion a year in 2022 and 2023, and FFO will recover to THB1.6-THB1.7 billion a year over the same period.

We expect the delays in handovers of construction sites and payments, as well as variation of orders over the course of large-scale public constructions, will continue. As a result, working capital needs should remain high. However, the debt to EBITDA ratio will likely drop to about 5 times during 2022-2023, as earnings recover. We project the ratio of FFO to debt to improve to 13%-14% over the same period. Despite the expectation of UNIQ's improving performance, the delayed biddings for public projects and intense competition remain significant downside risks.

Manageable liquidity

We expect UNIQ to manage its liquidity properly. About half of the total debts comprise short-term project financing from banks providing flexible debt repayment terms. UNIQ has THB1.8 billion in long-term loans coming due in 2021. These include THB0.8 billion in long-term loans from banks and THB1 billion in debentures. The former should be sufficiently covered by the expected FFO of about THB1 billion in 2021. UNIQ plans to refinance the debentures coming due worth THB1 billion with the issuance of new debentures. As of December 2020, UNIQ had cash and undrawn credit facilities of approximately THB1.4 billion in total as other sources of cash.

A key financial covenant of UNIQ's debentures requires the net interest-bearing debt to equity ratio to stay below 3.5 times. The company was compliant with this key financial covenant, with a ratio of about 1.9 times at the end of 2020. We believe the company will stay compliant with the financial covenant during the forecast period.

BASE-CASE ASSUMPTIONS

- UNIQ to secure new construction contracts for THB5-THB20 billion per year.
- Gross margin to range between 14%-18%.
- Capital spending to be THB1-THB1.5 billion per annum.

RATING OUTLOOK

The "negative" outlook embeds our expectation that UNIQ's earnings and financial profile will continue to deteriorate in 2021, given the current backlog and considerable amounts of receivables. We expect the company's performance to improve each year thereafter as we expect the company will be able to secure new contracts. However, uncertainties including the prolonged delays in public project biddings and intense competition remain the key risks.

RATING SENSITIVITIES

A rating downgrade could occur if UNIQ's financial profile materially deteriorates further from our expectations. This could be due to project delays, cost overruns, or inefficient working capital management, such as the scenario in which debt to EBITDA ratio stays above 5 times with no signs of recovery. Lower-than-expected amounts of new contracts could also weigh significantly on the ratings. In contrast, the rating outlook will be revised to "stable" if working capital management and profitability are in line with expectations and if UNIQ secures new construction contracts as targeted.

COMPANY OVERVIEW

UNIQ was founded in 1994 by Mr. Prasong Suviwattanachai and listed on the SET in 2007. The Suviwattanachai family remains the major shareholder, holding approximately 37% of the company's shares as of July 2020. The company is an E&C contractor, providing an extensive range of turnkey construction and related services for fundamental infrastructure such as roads, bridges, underpasses, highways, underground infrastructure, and mass transit systems and stations. It focuses on public sector projects in Thailand such as electric trains, double-track railways, and roads.

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS*

Unit: Mil. THB

	----------------------- Year Ended 31 December --------------------				
	2020	**2019**	**2018**	**2017**	**2016**
Total operating revenues	10,891	12,075	12,983	12,675	12,665
Earnings before interest and taxes (EBIT)	1,113	1,657	1,621	1,569	1,475
Earnings before interest, taxes, depreciation, and amortization (EBITDA)	2,286	2,652	2,854	2,755	2,377
Funds from operations (FFO)	1,393	1,662	2,027	2,072	1,786
Adjusted interest expense	792	725	617	452	381
Capital expenditures	3,334	1,783	409	428	891
Total assets	33,563	32,821	29,340	27,561	23,735
Adjusted debt	14,827	10,685	8,340	7,245	5,084
Adjusted equity	8,045	8,146	7,740	7,297	6,748
Adjusted Ratios					
EBITDA Margin (%)	20.99	21.96	21.98	21.73	18.77
Pretax return on permanent capital (%)	5.13	9.03	10.01	11.08	11.85
EBITDA interest coverage (times)	2.89	3.66	4.63	6.10	6.23
Debt to EBITDA (times)	6.49	4.03	2.92	2.63	2.14
FFO to debt (%)	9.40	15.56	24.31	28.60	35.12
Debt to capitalization (%)	64.83	56.74	51.87	49.82	42.97

* *Consolidated financial statements*

RELATED CRITERIA

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

Unique Engineering and Construction PLC (UNIQ)

Company Rating:	BBB+
Issue Ratings:	
UNIQ222A: THB2,000 million senior unsecured debentures due 2022	BBB
UNIQ232A: THB3,000 million senior unsecured debentures due 2023	BBB
Rating Outlook:	Negative

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