

EASTERN WATER RESOURCES DEVELOPMENT AND MANAGEMENT PLC

No. 95/2020

30 June 2020

CORPORATES

Company Rating:	A+
Issue Ratings:	
Senior unsecured	A+
Outlook:	Stable

Last Review Date: 26/06/19

Company Rating History:

Date	Rating	Outlook/Alert
23/01/08	A+	Stable
20/09/07	A+	Alert Developing
12/07/04	A+	Stable
29/06/04	A+	-

Contacts:

Suchana Chantadisai
suchana@trisrating.com

Chanaporn Pinphithak
chanaporn@trisrating.com

Wajee Pitakpaibulkij
wajee@trisrating.com

Wiyada Pratoomsuwan, CFA
wiyada@trisrating.com



WWW.TRISRATING.COM

RATIONALE

TRIS Rating affirms the company rating on Eastern Water Resources Development and Management PLC (EASTW) and the ratings on its outstanding senior unsecured debentures at “A+”, with a “stable” outlook. The ratings reflect EASTW’s strength as a key raw water provider with a comprehensive pipeline network in the Eastern Seaboard area, its reliable cash flow, and strong profitability. These strengths are partially offset by the ongoing drought and the slowdown of the Thai economy.

KEY RATING CONSIDERATIONS

Key raw water provider in the Eastern Seaboard

EASTW’s position as the key provider of raw water in the Eastern Seaboard underpins its strong business profile. Its integrated pipeline network facilitates the efficient allocation and channeling of water from multiple sources to service areas in Chonburi, Rayong, and Chachoengsao provinces. EASTW’s comprehensive network makes it uneconomical for any newcomer to compete in the company’s service areas. In addition to the large capital investment needed to build a pipeline, a new pipeline requires rights of way which would have to pass the approval of several government agencies.

Rising demand in EEC

Being a reliable raw water provider in the eastern region with almost 30 years of experience, EASTW has gained the opportunity to provide industrial water and fully integrated water services in the Eastern Economic Corridor (EEC) area. In 2018, EASTW signed two long-term contracts with Gulf P.D. Co., Ltd. (Gulf PD) and Amata Water Co., Ltd. (Amata water) to provide industrial water starting from 2021 onwards. These two contracts are expected to generate revenue of Bt240 million per annum.

The company also won the bidding to provide tap water and waste water treatment services to U-Tapao airport. EASTW has also gained opportunities to provide services outside the EEC.

Impact from drought

One unpredictable factor that affects water supplies is the climate. During the dry season or in periods of drought, water sources become depleted while feeding water from distant sources increases electricity costs. Apart from existing sources from the Royal Irrigation Department (RID), EASTW has developed its own reservoirs and sources raw water from private ponds, though the cost has been relatively higher.

The drought in Thailand became serious in 2019, with the lowest level of rainfall in the past 10 years. In 2019, the water storage volume of reservoirs in Chonburi and Rayong provinces fell dramatically from 2017-2018 level. EASTW’s total raw water costs per cubic meter (cu.m.) in 2019 rose by 15% from 2018 level. However, earnings before interest, tax, depreciation, and amortization (EBITDA) margin still stayed around 50% in 2019 and improved to 56% in the first three months of 2020.

As of 12 June 2020, the water storage volume of EASTW’s major water sources in Chonburi and Rayong provinces was improving but still low at approximately 23% of storage capacity, lower than the 48% recorded as of 14 June 2019. EASTW and the government have intensive plans to manage the

current water situation. However, as the rainy season has started, rainfall is picking up. The water sources are expected to be sufficient for demand throughout the year.

Strong profitability and predictable cash flow

EASTW's healthy financial profile is supported by its reliable cash flow and strong profitability. Its EBITDA has been in the range of Bt2.3-2.4 billion during 2015-2019.

Although the COVID-19 pandemic has affected the Thai economy and most business sectors, EASTW has experienced mild negative impacts from its customers. Water demand for households is predictable since water is necessary for daily use and its cost is considerably low compared with other costs of living. Raw water is also a critical material for production activities in the industrial sector. TRIS Rating expects EASTW's revenue to decline by 2% in 2020 before recovery in 2021-2022.

Investment projects to push up leverage

Under TRIS Rating's base case scenario, we expect EASTW's leverage to increase over the next three years. EASTW needs secure and sufficient supplies of water to cope with rising demand from its customers and to solve the drought situation.

EASTW plans capital expenditure of approximately Bt7.0 billion during the next three years. Around Bt4.4 billion will be spent in 2020 partly to support new industrial water users, Gulf PD and Amata water. The company will use the bulk of the capital expenditure to develop new pipelines, upgrade pumping stations, and enhance water development technology. We expect that EASTW's total debt to capitalization ratio to climb to 49.0% over the next three years. The ratio of funds from operations (FFO) to total debt will likely be lower than 20.0% with the EBITDA interest coverage ratio at 7-8 times during 2020-2022.

At the end of March 2020, EASTW's leverage and liquidity profile remained sound. The total debt to capitalization ratio was at healthy 40.3%. The FFO to total debt ratio was 23.8%, annualized from the trailing 12 months, while the EBITDA interest coverage ratio stood at 12.7 times for the first three months of 2020.

BASE-CASE ASSUMPTIONS

- Total revenues to decline by 2% in 2020 due to drought and COVID-19 and gradually grow by 4% in 2021 and 7% in 2022.
- Gross profit margin to stay in the 43%-45% range and EBITDA margin at 51%-53% in 2020-2022.
- Total capital spending to be Bt4.4 billion in 2020, Bt1.8 billion in 2021 and Bt680 million in 2022.

RATING OUTLOOK

The "stable" outlook reflects our expectation that EASTW's operations will remain resilient and continue to generate reliable streams of cash. TRIS Rating also expects the company to expand through the conservative use of leverage and maintain financial disciplines.

RATING SENSITIVITIES

A rating upside depends on whether EASTW can increase operating cash flow materially without weakening its balance sheet. A rating downside, on the other hand, could come from overly aggressive, debt-funded investments, resulting in the debt to capitalization ratio rising above 50% on a sustained basis.

COMPANY OVERVIEW

EASTW was established in 1992 by a Cabinet resolution. The government granted EASTW a mandate to develop and manage raw water distribution systems in the Eastern Seaboard area. As of May 2020, EASTW's major shareholders were the PWA (owning a 40.2% stake); Manila Water Company, Inc. (MWC; 18.7%); and the Industrial Estate Authority of Thailand (IEAT; 4.6%).

In 2019, EASTW extracted 332 million cubic meters (cu.m.) of raw water and supplied a total of 313 million cu.m., including internal use for tap water production. Currently, EASTW provides raw water in Chonburi, Rayong, and Chachoengsao provinces. The company has a strategy to focus on comprehensive water solutions, covering raw water, industrial water, waste water management, and recycled water.

EASTW, through its subsidiary Universal Utilities PLC (UU), provides tap water services in 13 areas with a total production capacity of 399,060 cu.m. per day. Excluding construction revenue under concession agreement, raw water sales accounted for 62.8% of the company's total revenue, while tap water services represented 33.2% of the total in 2019. In 2018, EASTW signed a 25-year contract with Gulf PD and a 30-year contract with Amata water to provide industrial water

of 21.9 million cu.m. per year and 5.5 million cu.m. per year, respectively. The revenue from these industrial water contracts is expected to be recognized from 2021 onwards. The company also won the bidding to provide tap water and waste water treatment services to U-Tapao airport under a 25-year concession.

KEY OPERATING PERFORMANCE

Table 1: EASTW's Total Revenue Breakdown by Line of Business

Line of Business		2015	2016	2017	2018	2019	Jan-Mar 2020
Raw water	%	66	62	57	57	61	61
Tap water	%	27	32	33	34	32	32
Engineering services and rental	%	5	4	4	4	3	4
Construction revenue under concession agreement	%	2	3	6	6	4	3
Total	%	100	100	100	100	100	100
Revenue from sale & service	Bt mil.	4,367	4,377	4,308	4,221	4,680	1,157

Source: EASTW

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS*

Unit: Bt million

	Jan-Mar 2020	-----Year Ended 31 December -----			
		2019	2018	2017	2016
Total operating revenues	1,160	4,701	4,235	4,335	4,395
Earnings before interest and taxes (EBIT)	424	1,472	1,542	1,666	1,761
Earnings before interest, taxes, depreciation, and amortization (EBITDA)	645	2,317	2,297	2,353	2,434
Funds from operations (FFO)	523	1,822	1,802	1,812	1,849
Adjusted interest expense	51	232	234	240	258
Capital expenditures	469	1,527	796	849	1,108
Total assets	22,097	21,181	20,141	19,483	19,860
Adjusted debt	7,662	7,161	6,511	7,131	7,420
Adjusted equity	11,330	11,014	10,805	10,430	10,048
Adjusted Ratios					
EBITDA margin (%)	55.55	49.28	54.23	54.28	55.37
Pretax return on permanent capital (%)	7.69 **	8.00	8.54	9.23	9.62
EBITDA interest coverage (times)	12.65	9.97	9.80	9.82	9.44
Debt to EBITDA (times)	3.32 **	3.09	2.83	3.03	3.05
FFO to debt (%)	23.76 **	25.44	27.67	25.41	24.92
Debt to capitalization (%)	40.34	39.40	37.60	40.61	42.48

* Consolidated financial statements

** Annualized from the trailing 12 months

RELATED CRITERIA

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

Eastern Water Resources Development and Management PLC (EASTW)

Company Rating:

A+

Issue Ratings:

EASTW226A: Bt1,200 million senior unsecured debentures due 2022

A+

EASTW256A: Bt1,200 million senior unsecured debentures due 2025

A+

Rating Outlook:Stable

TRIS Rating Co., Ltd.

Silom Complex Building, 24th Floor, 191 Silom Road, Bangkok 10500, Thailand Tel: 0-2098-3000

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