TPI POLENE PLC

No. 25/2021
15 March 2021

CORPORATES

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

Last Review Date: 20/08/20

Company Rating History:

Date	Rating	Outlook/Alert
25/03/20	BBB+	Stable
10/04/19	BBB+	Positive
02/10/12	BBB+	Stable

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RATIONALE

TRIS Rating affirms the company rating on TPI Polene PLC (TPIPL) and the ratings on TPIPL's outstanding senior unsecured debentures at "BBB+". TRIS Rating also maintains the outlook at "stable".

At the same time, TRIS Rating assigns the rating of "BBB+" to TPIPL's newly proposed issue of up to THB4 billion in senior unsecured debentures. The company intends to use part of the proceeds from the new debentures to refinance the bond which will mature in August 2021.

The ratings reflect TPIPL's strong market position in the domestic cement industry, a leading position in low-density polyethylene (LDPE) and ethylene vinyl acetate (EVA) market, solid cash flow by power purchase agreements (PPAs) with the Electricity Generating Authority of Thailand (EGAT), and the positive effect of business diversification. However, these strengths are held back by the cyclicality of the cement and plastic industries, the operational risks inherent in refuse-derived fuel (RDF) power plants, and investment risks associated with the Special Economic Zone (SEZ) development project. The ratings are also constrained by an expected rise in the company's financial leverage during investment periods and the high reliance on bond financing.

KEY RATING CONSIDERATIONS

Established position in the cement market

TPIPL remains the third-largest cement producer in Thailand, covering about 23% of industry-wide capacity. The company's competitive strengths are underpinned by its large business scale, vertical integration along with the cement production chain, and a broad range of product offerings such as cement, concrete, fiber cement, concrete roof tile, light weight concrete, and mortar. These strengths in the cement business are held back by various risks, including the industry cyclicality, price competition, capital-intensive investment, and cyclicality in coal price.

A leading position in LDPE and EVA

TPIPL is one of Thailand's leading LDPE and EVA producers with a production capacity of 158,000 tonnes per annum. TPIPL is part of the integrated petrochemical complex in Rayong province. TPIPL held about 20% domestic market share by capacity for LDPE. For EVA, TPIPL is the only producer in Thailand.

Over the past years, TPIPL has gradually moved away from low-margin commodity LDPE toward specialty grade EVA products which render higher margin. EVA revenue in the plastic segment has continuously increased, accounting for over 90% of the total. TPIPL plans to launch higher quality EVA products to strengthen its earnings. In addition, the company is a major producer of chemical products in Thailand, such as glue, ammonium nitrate, and nitric acid.

TPIPL's business risk in the plastic segment reflects the exposure to price volatility in petrochemical products and a few global competitors.

Reliable cash flow backed by PPAs

The ratings on TPIPL are largely strengthened by the strong credit profile of its core subsidiary, TPI Polene Power PLC (TPIPP). TPIPP is the largest waste-to-energy (WTE) power producer in Thailand. TPIPP owns and operates eight power plants with total installed capacity of 440 megawatts (MW). Of the total, four power plants (180 MW) carry three multi-year PPAs to sell a capacity of 163 MW to EGAT (rated “AAA/Stable” by TRIS Rating).

The PPAs largely mitigate demand risk and grant a favorable adder of THB3.50 per kilowatt-hour (kWh). The PPAs materially benefit TPIPL, providing secure long-term cash flow and improved earnings predictability. These business strengths are offset by operational risks from RDF-fired power plants, which stem from the unsteady supply of waste heat and varying quality of RDF. However, this has been counteracted by ongoing plant improvements and installation of three additional boilers in its power plants.

Business diversification

The ratings incorporate TPIPL’s diversified sources of revenue from three core businesses: construction materials (48% of total revenue in 2020), plastics (17%), and power generation (22%). However, in terms of cash generation, TPIPP has generated most of the group’s net cash flow or approximately 60% of earnings before interest, taxes, depreciation, and amortization (EBITDA) in 2020.

The diversification benefits from the power business meaningfully offset the volatile nature of the cement and plastic businesses and has helped stabilize TPIPL’s overall cash flow.

Seeking new PPAs to offset impact from adder expiration

The expiration of the tariff adder will impact upon the profitability and cash generation of TPIPL’s power business. The adders of the first two PPAs, totaling 73 MW, will expire in January and August 2022. The expiration of the adder will take full effect in 2023, reducing TPIPL’s EBITDA by around THB2 billion. Looking further ahead, TPIPL’s earnings will still be at risk of contraction as the adder of the largest PPA (90 MW) will expire in April 2025.

In our view, earnings sustainability of TPIPL’s power business will depend on the number of new PPAs TPIPP can obtain from now on. The company is striving to seek new project investments nationwide to replenish its dwindling earnings. Recently, the company won the bidding for a 9.9-MW WTE power plant in Songkhla province and secured a 20-year PPA with the contracted capacity of 7.92 MW. The tariff rate is THB5.78 per kWh for the first eight years and THB5.08 per kWh after that. The project renders tipping fees of THB400 per ton. The company is preparing to participate in bidding for 11 new WTE power plants, which will open for bidding during 2021-2022. The contracted capacities are in the range of 8-9.9 MW per plant. Additionally, the company is proposing to sell electricity produced by its RDF-fired power plant to the state-owned utility off-taker, with a contracted capacity of 40 MW. If the PPA is granted, TPIPP is expected to receive meaningful earnings to partially mitigate the impact of the adder expiration.

We believe that the company has a potential to attain several new power projects, underpinned by its expertise in operating WTE. TPIPP’s key management preliminarily estimates that each new WTE project can provide revenue of THB400-THB500 million per year and EBITDA of THB300-THB400 million per year. In addition, we view that success in obtaining new 40-MW PPA will be a positive factor since the RDF-fired plant is ready to generate electricity. For the downside risk, TPIPL’s efforts to secure additional contracts will be very challenging, given the intense bidding competition.

Anticipated earnings upside from efficiency enhancement

In addition to seeking new PPAs, TPIPL has undertaken a host of efficiency enhancement programs covering all business units, with a total investment of THB7.3 billion to support its long-term earnings. The key projects include a major overhaul of its existing cement plants, enhancing the use of RDF in the cement production by 25%-30% and capacity expansion of high-value added plastics and chemicals. The benefits from these projects are expected to be realized in 2021-2022. Top management expects these programs will generate additional EBITDA of around THB3 billion per annum.

We view TPIPL’s concerted efforts could potentially raise the group’s earnings. However, we have not fully taken the benefits into our base-case forecast, reflecting our conservative assessment. The actual benefits will need to be proven. TPIPL’s achievement in solidifying earnings is considered a positive factor on the ratings.

Risks associated with the SEZ project

We view that TPIPL’s early investment in the SEZ project in Songkhla province will expose the company to a range of risks. The project could take much time due to slow-moving bureaucracy. The Prime Minister recently reaffirmed the government’s commitments to the project and approved the Southern Border Provinces Administrative Centre (SBPAC) to proceed in accordance with the respective cabinet resolutions. So far the company plans to acquire a total 17,500 rai of land in potential areas where the project will be developed. The company has to date spent nearly THB10 billion and will spend about THB4.4 billion in the acquisition of remaining land. TPIPL’s land acquisitions have resulted in heavier debt load and higher interest burden. TPIPL’s management expects the core assets, such as sizable power plants, will commence its operations within five years. However, we view that the delay risk remains possible. In our forecast, we believe TPIPL will not make any additional investments in the SEZ project unless the company obtains official agreements from the authorities, such as new PPAs.

If the SEZ project is materialized, the company will need to spend of over THB100 billion for the project development. This amount of capital spending is material to TPIPL's balance sheet. In return for this large investment risk, TPIPL's management expects to make additional EBITDA of THB20 billion per year when the SEZ project is fully completed. We believe TPIPL would need to seek capable partners or come up with a suitable financing scheme to avoid an overleveraged structure.

Satisfactory performance in 2020

In 2020, TPIPL's overall performance improved from the previous year despite severe impacts from the Coronavirus Disease 2019 (COVID-19) pandemic. Its earnings continue to be driven by its strong power business. Compared with the last year, total revenue dropped to THB35.3 billion or down by 7.3% due mainly to the declining cement price. However, EBITDA was THB9.5 billion, up by 24.8%, while funds from operations (FFO) were THB7.5 billion, up by 33.6%.

TPIPL's earnings soared chiefly due to the wider spread of plastics in its petrochemical business. Although TPIPL's cement business was affected by sluggish demands in Thailand, its profit margin improved thanks to a drop in coal prices and improved efficiency of the cement plants. The power plants selling power to EGAT continued to perform well with higher and more stable utilization rate after the company completed installation of two additional boilers in the second half of 2020. The third boiler is expected to be installed completely in the first quarter of 2021.

Rising leverage to support potential investments

In our base case forecast, we expect cement demand to gradually be restored in the second half of 2021 onwards. However, TPIPL's profit margin in cement and plastic segments is still subject to coal price, spread of plastics, and benefits of efficiency enhancement programs the company is undertaking. As for the power segment, the new 9.9-MW WTE project TPIPL recently secured is expected to commence operations in late 2023. We expect TPIPL should be able to secure additional PPAs. In our base case, we assume TPIPL would win bid for several new WTE projects, with a combined capacity of about 60 MW. However, we do not incorporate the new 40-MW PPA from its RDF-fired power plant. With respect to the SEZ project, we do not assume any additional investments, except for the purchase of the remaining land.

We expect TPIPL's debt will increase following potential investments. The company's leverage will gradually rise over the course of development of new WTE power projects but it should decline substantially after all projects begin commercial operations. Over the forecast period, total revenue is expected to stay in the range of THB37-THB39 billion. EBITDA is likely to maintain in the range of THB9-THB9.5 billion in 2021 before gradually dropping to THB7.5 billion in 2023 because of the adder expirations. However, we expect EBITDA will rebound to THB9 billion in 2024 once all new power plants are in operation. At the same time, we expect FFO will fall to THB5.5-THB6.5 billion in 2021-2022 from THB7.3 billion in 2020. FFO will drop to about THB5 billion in 2023 but should bounce back to THB6.2 billion in 2024.

The net debt to EBITDA ratio will gradually rise to about 7-8 times in 2023 during the construction of several new power plants, from 5.8 times in 2020. The ratio will improve, considerably reducing to about 6.5 times in 2024. At the same time, the ratio of FFO to net debt is likely to fall to 7%-8% in 2021-2023 from 13% in 2020 before rebounding to about 10% in 2024. The net debt to capitalization ratio is projected to rise to the range of 50%-55%.

High reliance on bond financing

Due to the management's preference and the favorable bond market over the past several years, TPIPL continues to use bonds as a main source of financing. The company's debentures financing has continued to account for 80% of total outstanding debt. Given its high reliance on bond financing, we view the company's refinancing ability is subject to the market condition.

TPIPL has debentures worth THB9.6 billion coming due in April 2021. The company has prudently prepared sufficient liquidity to cover the repayment of the debentures. At the end of 2020, TPIPL had cash on-hand and short-term investments worth THB10 billion. TPIPL already received THB4 billion proceeds in March 2021, following the recent success in issuance of new debentures. We expect TPIPL to continue facing refinancing risks from a series of debentures issuances. We believe this risk will be mitigated by its good record of accessing the debt capital market.

TPIPL continues to comply with the financial covenant of its debentures, which requires the interest-bearing debt to equity ratio to stay below 1.5 times. As of December 2020, the ratio stood at 1.19 times. However, we expect the headroom from covenants will become smaller, considering the prospects of its sizable investments.

BASE-CASE ASSUMPTIONS

- Revenues from the cement segment to grow by 1%-2.5% during 2021-2023.
- Revenues from the plastic segment to be flat during the projected period in 2021-2023.
- Revenues from the power segment to begin to decline in 2022 and 2023.
- EBITDA margin to decline to 20% from 23% during 2021-2023.
- Capital expenditures during 2021-2023 to total THB22 billion.
- Dividend payout to be at 50%

RATING OUTLOOK

The "stable" outlook reflects our expectation that TPIPL's competitive positions in the cement and plastic businesses will be maintained. At the same time, its power business will continue to exhibit satisfactory performance and maintain its cash flow contribution. We also expect the company will successfully secure new power projects to partially counterbalance the drop-off in cash flow after the adder expiration. Also, its operating performance and financial leverage will remain in the forecast range.

RATING SENSITIVITIES

The prospect of a rating upgrade is limited in the near term but it could emerge if TPIPL has proven to materialize its efficiency enhancement measures and successfully secured new power purchase agreements. These will enable TPIPL to considerably fortify its earnings as the company expects. Other factors influencing an upgrade are the debt to EBITDA ratio that falls below 6 times for a sustained period and TPIPL's diversification of its sources of borrowings. Positive rating factors could also develop from financial deleveraging.

The ratings and/or outlook could be revised downward if TPIPL's net debt to EBITDA ratio stays above 8 times for a lengthy period. The rating downside could stem from deterioration of the cement business, weaker-than-expected performance of power plants, as well as large debt-funded investments. A large equity loss from pending legal claims could also trigger a negative rating action.

COMPANY OVERVIEW

TPIPL was founded by the Leophairatana family in 1987. Following the financial crisis in 1997, TPIPL signed a Master Restructuring Agreement (MRA) and entered a debt restructuring program in July 2000. The company exited the rehabilitation process in 2009. The Leophairatana family is the major shareholder, owning approximately 58% of the company. The family members have served as the company's board members and management team since the firm was founded.

TPIPL operates in various industries: construction materials, plastics, and power generation. The construction material segment produces and sells clinker, cement, mortar, concrete, fiber cement, and concrete roof tiles. The plastic segment manufactures and sells LDPE and EVA products. The power segment generates electricity using mainly RDF and waste heat recovery. The company sells the power to EGAT and supplies within the group. The company's other products include ammonium nitrate, nitric acid, health care products, organic fertilizer, and synbiotics.

TPIPL, through TPIPP, has engaged in the development of the SEZ, a mega industrial project initiated by the government to develop the economy in the southern part of Thailand. The project, which covers approximately 17,000 rai of land in Chana district, Songkhla province, will comprise deep-sea ports, industrial estates, and large power plants. TPIPL aims to tender for the development of the SEZ project with an eye on large gas-fired power plants. In preparation for the tender, TPIPL plans to acquire a total of 17,500 rai of land in the surrounding areas.

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS*

Unit: Mil. THB

	---------------------Year Ended 31 December -------------------				
	2020	**2019**	**2018**	**2017**	**2016**
Total operating revenues	36,027	38,758	36,851	30,726	30,735
Earnings before interest and taxes (EBIT)	6,310	4,311	3,002	567	1,156
Earnings before interest, taxes, depreciation, and amortization (EBITDA)	9,554	7,650	5,889	3,318	3,706
Funds from operations (FFO)	7,285	5,576	3,869	1,801	2,235
Adjusted interest expense	2,343	2,096	1,802	1,758	1,774
Capital expenditures	11,471	9,905	7,409	7,536	6,259
Total assets	123,909	114,368	110,488	103,178	92,618
Adjusted debt	55,879	51,634	45,041	37,243	45,124
Adjusted equity	52,172	51,493	50,937	52,086	36,755
Adjusted Ratios					
EBITDA margin (%)	26.5	19.7	16.0	10.8	12.1
Pretax return on permanent capital (%)	5.6	4.1	3.0	0.6	1.3
EBITDA interest coverage (times)	4.1	3.7	3.3	1.9	2.1
Debt to EBITDA (times)	5.8	6.7	7.6	11.2	12.2
FFO to debt (%)	13.0	10.8	8.6	4.8	5.0
Debt to capitalization (%)	51.7	50.1	46.9	41.7	55.1

* *Consolidated financial statements*

RELATED CRITERIA

- Group Rating Methodology, 13 January 2021
- Rating Methodology – Corporate, 26 July 2019
- Key Financial Ratios and Adjustments, 5 September 2018

TPI Polene PLC (TPIPL)

Company Rating:	BBB+
Issue Ratings:	
TPIPL214A: THB1,600 million senior unsecured debentures due 2021	BBB+
TPIPL214B: THB8,000 million senior unsecured debentures due 2021	BBB+
TPIPL218A: THB3,580 million senior unsecured debentures due 2021	BBB+
TPIPL221A: THB3,530 million senior unsecured debentures due 2022	BBB+
TPIPL224A: THB1,200 million senior unsecured debentures due 2022	BBB+
TPIPL228A: THB3,745 million senior unsecured debentures due 2022	BBB+
TPIPL231A: THB3,000 million senior unsecured debentures due 2023	BBB+
TPIPL231B: THB4,382.7 million senior unsecured debentures due 2023	BBB+
TPIPL234A: THB2,640.5 million senior unsecured debentures due 2023	BBB+
TPIPL244A: THB4,127 million senior unsecured debentures due 2024	BBB+
TPIPL24NA: THB3,515.3 million senior unsecured debentures due 2024	BBB+
TPIPL251A: THB2,888 million senior unsecured debentures due 2025	BBB+
TPIPL256A: THB4,000 million senior unsecured debentures due 2025	BBB+
TPIPL25NA: THB3,410.7 million senior unsecured debentures due 2025	BBB+
Up to THB4,000 million senior unsecured debentures due within 5 years	BBB+
Rating Outlook:	Stable

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