

# EASTERN SUGAR AND CANE PLC

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## CORPORATES

**Company Rating:** BBB  
**Outlook:** Stable

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## RATIONALE

TRIS Rating assigns the company rating to Eastern Sugar and Cane PLC (ESC) at “BBB” with a “stable” rating outlook. The rating reflects ESC’s long track record in the sugar industry, diverse sources of income, and conservative financial policies. Nevertheless, these strengths are partially offset by ESC’s small size and the inherent volatility faced by producers of commodity products like sugar.

## KEY RATING CONSIDERATIONS

### Long track record

ESC’s competitive edge is underpinned by its track record of over 60 years in the sugar industry. In 2018, export sales made up 90% of revenue in the sugar segment. All of ESC’s export customers are international traders.

ESC currently focuses on high-quality products such as Very High Polarization sugar (VHP) and refined sugar. The company is one of just eight plants in Thailand to have received the Bonsucro standard certificate. Premium sugar yields a higher profit margin and attracts more customers.

### Geographical advantage of production site

Sugarcane is the main raw material used to produce sugar. Sugarcane is a cool-weather crop grown primarily in eastern and northeastern Thailand. In the eastern region, ESC is the only sugar producer in Sa Kaeo province; other sugar mills are in Chonburi province. Since it is the only sugar producer in Sa Kaeo province, ESC does not normally have to compete with other producers to secure sufficient supplies of sugarcane to feed its mills. ESC also enjoys strong and strengthening relationships with sugarcane growers. The company offers broad-based support to growers, including advances of cash and fertilizer, development of planting techniques, advanced irrigation techniques, and breeding and harvesting tools.

### Diversified sources of income

ESC has expanded along the sugar value chain in order to maximize the utilization of sugarcane and the by-products of the sugar manufacturing process. ESC’s major sugar-related businesses are electricity generation and ethanol production.

ESC’s power plants have a combined installed power generation capacity of 123.6 megawatts (MW). Bagasse, a by-product of sugar production, is used as biofuel for electricity generation. The company sells electricity to two state-owned enterprises under long-term power purchase agreements (PPA). The Electricity Generating Authority of Thailand (EGAT) purchases 40 MW of electricity under the Small Power Producer (SPP) scheme while the Provincial Electricity Authority (PEA) buys 11 MW under the Very Small Power Producer (VSPP) scheme.

ESC has an ethanol production capacity of up to 150,000 litres per day. Buyers of ethanol are the major oil companies in Thailand.

Revenue from the energy segment (electricity and ethanol) has increased steadily and now comprises a significant portion of total revenue. In 2018, revenue from the energy segment accounted for 24% of ESC’s total revenue; the sugar segment made up the balance.

### Softer earnings and profitability expected

ESC has achieved relatively stable profitability despite the cyclical nature of sugar prices and sugarcane supplies thanks to the steady cash flow generated from sales of electricity to EGAT and PEA. The earnings before interest, tax, depreciation, and amortization (EBITDA) margin hovered in the 15%-19% range during 2014-2018.

Nonetheless, given the current worldwide oversupply of sugar, TRIS Rating forecasts a drop in ESC's revenue in 2019-2020. EBITDA margin could fall below 15%. In the first nine months of 2019, EBITDA margin was reported at 15%.

### Moderate leverage and cash flow protection

Under TRIS Rating's base-case scenario, we expect ESC's leverage to gradually drop over the next three years. No major capital expenditures are expected since the investments needed for new plants and a capacity increase were already made during the past five years.

ESC plans capital expenditures of less than Bt1.00 billion annually during the next three years. The majority of the capital expenditures will go to develop a new packaging line, implement a new software system, and buy sugarcane harvesters. The debt to capitalization ratio would be less than 60% (it was 57% in September 2019).

TRIS Rating assesses ESC's liquidity as adequate. The ratio of funds from operations (FFO) to total debt will likely be lower than 20% over the next three years. We expect the EBITDA interest coverage ratio will range around 4-7 times during 2019-2021.

### BASE CASE ASSUMPTIONS

- Revenues in 2019 to drop by 5% and drop slightly in 2020, before recover in 2021.
- Process improvements to gradually push up the EBITDA margin from 12% to 18% over the forecast period.
- Capital expenditures of Bt1.00 billion in 2019 and Bt700 million annually during 2020 and 2021.

### RATING OUTLOOK

The "stable" outlook reflects our expectation that ESC will maintain its competitive position in the Thai sugar industry. The revenue contribution from the energy segment will to some extent offset the volatility in the sugar business.

### RATING SENSITIVITIES

A rating upside case could occur if ESC continues delivering steady, satisfactory operating performance while maintaining an acceptable capital structure over the next couple of years. On the other hand, the rating downside case could emerge if profitability and earnings fall short of expectations. Any overly aggressive, debt-funded investments that would weaken the debt to capitalization ratio would also be a negative factor for the rating.

### COMPANY OVERVIEW

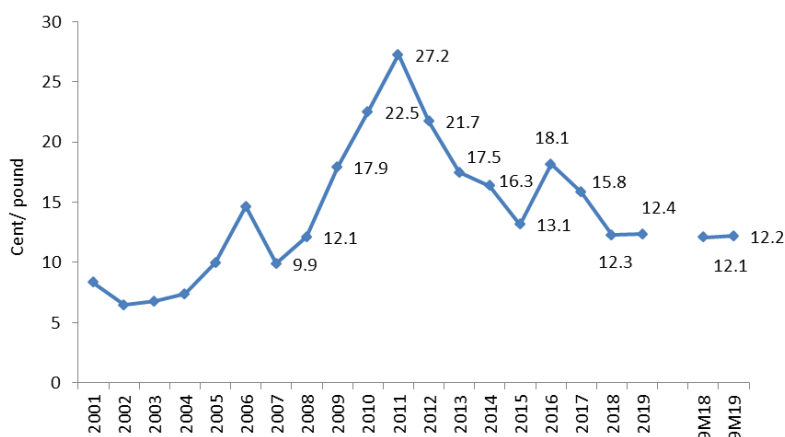
ESC was established in 1959 by the Wattanavekin family. As of December 2019, the Wattanavekin family collectively held 98.6% of the company's shares.

ESC's first sugar mill, located in Pluak Daeng, Rayong province, had a production capacity of 12,000 tonnes of cane per day (TCD). In 1994, the company relocated to Watthana Nakhon, Sa Kaeo province. Current production capacity is 40,000 TCD. ESC received approval in July 2018 to build a second mill at Wang Sombun, Sa Kaeo province. The new mill has a capacity of 18,000 TCD. The first phase of 8,000 TCD started up in December 2018.

ESC procured 4.3 million tonnes of sugarcane in the 2018/2019 production period and produced 492,482 tonnes of sugar. For the 2018/2019 production period, ESC's market share, in terms of tonnes of sugar produced in Thailand, was 3.4%. For comparison, the two market leaders held market shares of around 20% and 16.6%, respectively.

ESC sells sugar in two package sizes; 50 kilograms (kg) for domestic sales and 100 kg for export sales. Currently, ESC sells white and refined sugar in the domestic market. It exports raw sugar, VHP sugar, and refined sugar.

ESC's sugar-related businesses include the production of electricity, ethanol, and fertilizer, as well as research and development and logistics services.

**KEY OPERATING PERFORMANCE**
**Chart 1: Raw Sugar Price Worldwide**


Note: Monthly prices of Futures Contract No.11

Source: New York Board of Trade, United States Department of Agriculture (USDA)

**Table 1: Sugar Production in Thailand**

Unit: Million tonnes

Sugar Producer	Growing Season					
	2013/2014	2014/2015	2015/2016	2016/2017	2017/2018	2018/2019
Mitr Phol	2.30	2.30	1.96	1.98	2.73	2.92
Thai Roong Ruang	1.75	1.60	1.37	1.42	2.13	2.42
KSL Group	0.91	0.91	0.77	0.72	1.20	1.14
Thai Ekkalak	1.06	0.99	0.72	0.94	1.19	1.03
Wangkanai	0.70	0.56	0.51	0.39	0.79	0.69
Banpong	0.46	0.44	0.44	0.44	0.52	0.58
Kumpawapee	0.37	0.40	0.30	0.28	0.41	0.39
Buriram Sugar	0.21	0.23	0.24	0.25	0.38	0.35
Others	3.57	3.87	3.47	3.61	5.36	5.06
<b>Total</b>	<b>11.33</b>	<b>11.30</b>	<b>9.78</b>	<b>10.03</b>	<b>14.71</b>	<b>14.58</b>

Source: Office of the Cane and Sugar Board (OSCB)

**Table 2: ESC's Revenue Breakdown by Business**

Unit: %

Product	2014	2015	2016	2017	2018
Sugar sales	71	70	74	74	66
Ethanol sales	12	13	12	11	15
Electricity sales	8	8	6	7	9
Fertilizer sales	6	6	5	5	6
Service and others	3	3	3	3	4
<b>Total sales</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>
<b>Total sales (Bt million)</b>	<b>6,530</b>	<b>7,091</b>	<b>7,815</b>	<b>8,472</b>	<b>7,897</b>

Source: ESC

## FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS\*

Unit: Bt million

	-----Year Ended 31 December -----				
	2018	2017	2016	2015	2014
Total operating revenues	7,982	8,557	7,911	7,182	6,629
Earnings before interest and taxes (EBIT)	538	919	745	456	537
Earnings before interest, taxes, depreciation, and amortization (EBITDA)	1,277	1,604	1,368	1,051	1,076
Funds from operations (FFO)	1,042	1,294	1,128	766	875
Adjusted interest expense	228	225	203	265	244
Capital expenditures	1,780	973	1,588	685	587
Total assets	13,527	12,038	10,525	10,791	10,240
Adjusted debt	6,313	4,417	4,926	5,622	5,232
Adjusted equity	5,414	5,072	4,460	3,942	3,778
<b>Adjusted Ratios</b>					
EBITDA margin (%)	15.99	18.75	17.29	14.63	16.23
Pretax return on permanent capital (%)	4.99	9.51	7.77	4.86	6.40
EBITDA interest coverage (times)	5.60	7.13	6.72	3.97	4.41
Debt to EBITDA (times)	4.95	2.75	3.60	5.35	4.86
FFO to debt (%)	16.51	29.30	22.90	13.63	16.72
Debt to capitalization (%)	53.83	46.55	52.48	58.79	58.07

\* Consolidated financial statements

## RELATED CRITERIA

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

## Eastern Sugar and Cane PLC (ESC)

<b>Company Rating:</b>	BBB
<b>Rating Outlook:</b>	Stable

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