

# RIGHT TUNNELLING PLC

No. 9/2022  
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## CORPORATES

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

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## RATIONALE

TRIS Rating assigns a company rating of “BBB-” with a “stable” outlook to Right Tunnelling PLC (RT). The rating reflects RT’s competitive strengths and well-established track record in tunnel and shaft works. Conversely, the rating is constrained by RT’s relatively small scale of business and narrow scope of service offerings. The rating is also tempered by the severe competition in the engineering and construction (E&C) industry, the risk of delays in public construction project bidding, and RT’s rising financial leverage.

## KEY RATING CONSIDERATIONS

### Competitive strengths in excavation works

As a leading geotechnical construction company, RT is best known for its expertise in open and underground rock excavation. The company focuses on tunnel and shaft works, dam construction, hydro power plants, pipe jacking, and horizontal directional drilling. RT’s competitive strengths are built from its experienced management team, engineers, and geologists, as well as wealth of machinery and equipment. RT generally undertakes public construction projects. In some projects, the company serves as a sub-contractor for top-tier construction companies, charting the path to take on larger projects. RT has placed emphasis on building up its bidding qualifications, which have enabled the company to undertake larger construction works, expand the types of projects, and enlarge its client base over the past years.

### Well-established track record

RT has a well-established track record of successful project execution. Some projects are viewed as challenging in terms of geotechnical engineering. The company’s past projects include tunnelling the diversion and power waterways of Nam Ngum 2 hydropower and major civil works for the powerhouse of Xayaburi hydropower plant. These construction works are part of the large-scale hydropower plants in the Lao People’s Democratic Republic (Lao PDR), and both commenced operations ahead of schedule.

In addition, RT is about to complete the tunnelling works of the Dual-Track Rail Route Project for the Northeastern Line (Map Kabao-Thanon Chira Junction), which marks the longest rail tunnel in the country. We view RT’s competitiveness in its fields of expertise will continue to be the key strength supporting the company in winning new projects.

### Small business scale, but on growth trajectory

RT’s competitive strengths are offset by its small business scale. Across all construction contractors rated by TRIS Rating, RT is the smallest operator, in terms of revenue and asset base. We view the small scale of business as a significant constraint in bidding and financing, leading to low financial flexibility to weather unforeseen difficulties. In addition, RT’s revenue stream relies heavily on public constructions that are prone to project delays.

However, we expect RT to deliver a streak of healthy earnings, aided by an encouraging outlook for public-sector construction work in the next few years. We maintain our expectation that the government will continue in its efforts to upgrade the country’s infrastructure. We expect several potential projects undertaken by government agencies will involve excavation works. Such agencies include the State Railway of Thailand, the Royal Irrigation

Department, the Department of Highways, and the electricity authorities. Considering its expertise in geotechnical work, RT is in a good position to benefit from these public construction projects, particularly dual-track railways and underground cables.

In recognition of the prospects of future business opportunities, we forecast the company will scale up its revenue to a fresh record in the range of THB3-THB4 billion a year during 2022-2024. Its earnings before interest, taxes, depreciation, and amortization (EBITDA) should range from THB400-THB500 million per year.

#### **Highly susceptible to severe competition**

In our view, RT is highly susceptible to the cyclical and severe competition of the E&C industry, given its narrow scope of service offerings. Tunnel and shaft construction works contributed the majority of RT's construction revenue, at 55%-65%, over the past three years. Scarcity of new bidding for this type of work could adversely affect the company's performance.

Despite the positive outlook of public construction activities, we have witnessed repeated delays in the bidding and awarding of much-anticipated projects for various reasons. These include certain changes in the project master plan, disputes over the contract bidding process, prolonged government decision-making process, and delays in contract negotiation. Severe competition among contractors persists and weighs negatively on the rating. Most projects are awarded through competitive bidding, which constrains contractors' profit margins. New waves of Coronavirus Disease 2019 (COVID-19) outbreaks remain a serious threat to construction activities.

#### **Heavy concentration of major projects**

RT's operating results have been dominated by a few large projects. Revenue from the three largest projects made up almost 70% of total revenue over the past three years. The three largest projects under construction accounted for about 65% of its construction backlog as of September 2021. Failure to complete one large project or any significant disruption to the project could result in a material impact on operating performance.

We forecast RT's profit margins to likely remain volatile, due mainly to its small business scale and high dependency on a few large projects. The company needs to secure a number of new contracts with acceptable margins to attain sufficient gross profit to cover operating expenses. RT's EBITDA margin (EBITDA as a percentage of revenue), rose remarkably to 19%-21% during 2019-2020, from the past levels of 8%-11%, as one large project delivered superior profit margin. We expect RT's EBITDA margin over the next three years to fall to normal levels as the high-margin project is near completion.

Like other domestic contractors, RT has been hurt by an array of direct impacts from the COVID-19 pandemic, such as the temporary closure of construction workers' camps, disrupted supply of goods and materials, and delay of work progress. RT's profitability was also pressured by a spike in the prices of some materials and a contracted supply of labor. In our base-case forecast, we project its EBITDA margin to be 11%-13% during 2022-2024.

#### **Financial leverage on uptrend**

RT's gearing increased considerably in the first nine months of 2021. The company's debt to EBITDA ratio surged to 3.2 times, from a level below 1 time in 2020, when the company made an Initial Public Offering (IPO). A large sum of unbilled receivables, largely with respect to the Mae Taeng-Mae Ngat Diversion Tunnel Project, escalated its working capital needs and debt levels. The debt to capitalization ratio stood at 42.8% as of September 2021, compared with 27.4% as of 2020.

Over the forecast period, we expect RT's leverage to remain at current levels, considering its strategy to grow its revenue base. RT aims at securing larger infrastructure construction contracts, which should help enlarge its backlog and revenue base. In contrast, working capital needs will likely increase as large-scale public infrastructure projects are prone to circumstances that lead to delays in project completion, such as delayed handovers of construction sites, revisions of project master plans, and remedial work.

As a result, RT's debt to EBITDA ratio will unlikely revert to 1-2 times as seen in the recent past. In our base-case forecast, we project RT's debt to EBITDA ratio to rise towards 3.5 times during 2022-2024. Funds from operations (FFO) should range from THB300-THB380 million per year. We expect the ratio of FFO to debt to remain above 20% and the debt to capitalization ratio to range from 47%-54% over the forecast period.

#### **Debt Structure**

As of September 2021, RT's consolidated debt was THB1.3 billion, all of which was considered priority debt, comprising secured debt owed by RT. The priority debt to total debt ratio is 100%, suggesting that RT's unsecured creditors are significantly disadvantaged to its priority debt holders with respect to claims against the company's assets.

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### Liquidity stays manageable

We expect RT to manage its liquidity properly. As of September 2021, about 70% of total debts comprised short-term project finances from banks providing flexible debt repayment terms. Given RT's high capability in project execution and the creditworthiness of project owners, we expect RT should be able to rollover its short-term debts. At the same time, RT had THB183 million in long-term loans and financial leases coming due in the next 12 months, which should be sufficiently covered by the expected FFO of about THB300 million. Moreover, RT had cash and undrawn credit facilities of THB86 million in total as other sources of liquidity.

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### BASE-CASE ASSUMPTIONS

- RT to secure new construction contracts for THB3-THB4 billion per year during 2022-2024.
- Total operating revenue to range from THB3-THB4 billion per year.
- EBITDA margin to range from 11%-13%.
- Total capital spending to be THB300-THB600 million per annum.

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### RATING OUTLOOK

The "stable" outlook reflects our expectation that RT will maintain its competitive edge and secure new projects. We also expect performance and financial leverage will be at the levels in line with our forecast. Its debt to EBITDA ratio should range from 3-3.5 times.

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### RATING SENSITIVITIES

A rating upgrade could occur if RT's cash flows and leverage improve significantly. In contrast, downward revision to the rating could develop if RT's performance comes in considerably below our expectations or if its financial profile deteriorates substantially, possibly due to significant project delays, cost overruns, and inefficient working capital management.

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### COMPANY OVERVIEW

RT was founded in 2000 by Mr. Chawalit Tanomtin and listed on the Stock Exchange of Thailand (SET) in 2020. Mr. Chawalit Tanomtin, the founder, remains the major shareholder, holding approximately 16% of the company's shares as of August 2021. The company is a contractor specializing in geotechnical works, covering tunnel and shaft construction, dam construction, hydro power plants, pipe jacking, and horizontal directional drilling. RT is also engaged with slope protection and stabilization, earth and rock excavation, and geological exploratory drilling services. Revenue from tunnel and shaft construction has accounted for 55%-65% of total revenue over the last three years.

**KEY OPERATING PERFORMANCE**

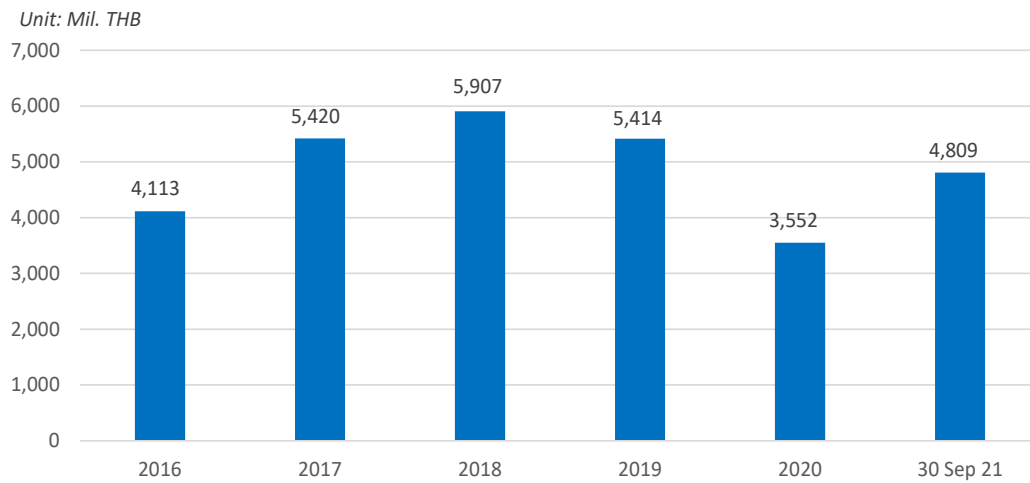
**Table 1: Construction Revenue Breakdown by Type of Project**

Unit: %

Type of Project	2016	2017	2018	2019	2020	Jan-Sep 2021
Tunnel & Shaft	40	33	65	61	59	53
Dam	11	7	1	2	8	18
Hydro Power	36	41	16	4	1	1
Pipe Jacking & Horizontal Directional Drilling	4	13	11	11	12	15
Others	10	6	7	22	20	13
<b>Total</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>

Source: RT

**Chart 1: Backlog Movement**



Source: RT

**FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS\***
*Unit: Mil. THB*

	Jan-Sep 2021	-----Year Ended 31 December -----			
		2020	2019	2018	2017
Total operating revenues	1,930	2,860	2,351	1,882	2,472
Earnings before interest and taxes (EBIT)	106	364	230	(38)	101
Earnings before interest, taxes, depreciation, and amortization (EBITDA)	223	550	500	203	233
Funds from operations (FFO)	181	428	382	151	195
Adjusted interest expense	39	68	75	47	31
Capital expenditures	29	28	135	238	189
Total assets	3,952	4,050	3,731	2,999	2,519
Adjusted debt	1,012	525	1,155	797	389
Adjusted equity	1,351	1,389	587	457	530
<b>Adjusted Ratios</b>					
EBITDA margin (%)	11.56	19.24	21.26	10.76	9.42
Pretax return on permanent capital (%)	6.59 **	15.66	12.67	(2.87)	10.11
EBITDA interest coverage (times)	5.70	8.09	6.68	4.30	7.51
Debt to EBITDA (times)	3.19 **	0.95	2.31	3.93	1.67
FFO to debt (%)	25.66 **	81.52	33.04	18.96	50.25
Debt to capitalization (%)	42.83	27.44	66.29	63.56	42.31

\* Consolidated financial statements

\*\* Adjusted with trailing 12 months

**RELATED CRITERIA**

- Key Financial Ratio and Adjustments for Corporate Issuers, 11 January 2022
- Issue Rating Criteria, 15 June 2021
- Rating Methodology – Corporate, 26 July 2019

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**Right Tunnelling PLC (RT)**

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

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