

Press Release

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TRIS Rating Assigns "A-/Stable" Rating to Senior Unsecured Debt Worth Up to Bt6,000 Million of "CK", Replacing Recent Debt of Up to Bt4,000 Million

TRIS Rating has assigned a rating of "A-" to the proposed issue of up to Bt6,000 million in 12 years senior unsecured debentures of CH. Karnchang PLC (CK). At the same time, TRIS Rating has affirmed the company rating of CK and the ratings of CK's outstanding senior unsecured debentures at "A-". The outlook remains "stable". The new issue rating replaces the issue rating previously assigned on 9 May 2017, following CK's request to increase the issue size to up to Bt6,000 million, from Bt4,000 million. The company will use the proceeds from the new debentures to repay some of its existing loans. The ratings reflect CK's position as a top-tier contractor, its ability to undertake large-scale and sophisticated construction projects, as well as the synergy and financial flexibility the company gains from its strategic investments. These strengths are partially offset by the cyclical nature and stiff competition in the engineering and construction (E&C) industry, as well as the company's high financial leverage.

The "stable" outlook reflects TRIS Rating's expectations that CK will remain highly competitive in securing new projects in the face of forthcoming infrastructure projects. CK will be able to sustain its operating margin above 6% on average despite a stiff competition and the total debt to capitalization ratio staying below 65% over the next three years.

A credit upside is possible if CK could significantly enhance cash flow protection by generating stronger-than-expected funds from operation, as well as maintain its debt to capitalization ratio below 60% for a sustained period. A credit downside will be caused by the significant cost overruns in major projects or unanticipated, extensive financial support provided to its affiliates, which would markedly hurt CK's cash flow.

Established in 1972 by the Trivisvavet family, CK initially focused on the public work projects for government agencies. The company later greatly expanded its scope of work and became a listed company on the Stock Exchange of Thailand (SET) in 1995. CK has a long-established presence in the E&C sector with experience and expertise in all kinds of construction, ranging from general civil works to highly sophisticated projects.

CK's revenue in 2016 was record-high at Bt45.8 billion, soaring from Bt34.8 billion in 2015. The hefty increase of 31.4% in revenue was largely a result from the contribution from the Xayaburi hydropower dam project, which accounted for 53% of the total revenue. CK was awarded an additional contract worth Bt19.4 billion to enhance environmental aspects of the project. Despite a significant amount of additional recognized revenue, CK, as a project sponsor, needs to finance the additional construction in the form of a sponsor loan to the project. CK provides sponsor loan to the project company, Xayaburi Power Co., Ltd. (XPCL), for the amount of Bt13.5 billion, with the schedule for the full loan repayment by 2031. XPCL will repay loan and interest from earnings after the commercial operation date, which is scheduled in 2019. The loan repayment risk thus is tied to the performance of XPCL. CK's profitability in 2016, however, was slightly lower than TRIS Rating's expectation. The gross profit margin fell to 7.2%, from 8.2% in 2015 due to the lower gross profit margin from the additional works in the Xayaburi project.

The ratings reflect CK's leading position in Thailand's E&C industry. CK is one of the top three contractors listed on the SET, based on revenue. The ratings also recognize its proven record of completing large-scale infrastructure projects and specialized construction projects. CK is amongst a few domestic contractors capable of undertaking large and sophisticated projects. In late 2016, CK won three contracts for the construction of the Mass Rapid Transit (MRT) Orange Line project, worth totally about Bt47 billion under the name of CKST Joint Venture. CKST Joint Venture is held 60% by CK and 40% by Sino-Thai Engineering & Construction PLC (STEC). CK secured a sizable backlog of Bt83.4 billion as of December 2016. The major projects in the backlog include the Xayaburi hydropower dam project worth Bt27.1 billion, the MRT Orange Line project contracts 1, 2, and 5, worth a combined value of Bt26.3 billion, and the double-track railroad project from the Chira junction to the Khon Kaen section worth Bt13 billion. These three projects account for 80% of the total backlog value. On the strength of its market presence, CK is poised for the forthcoming infrastructure projects.

Moreover, the ratings take into consideration the synergy and financial flexibility the company gains from its strategic investments. CK's business model is to invest in infrastructure projects to augment its primary business as an E&C contractor. CK holds stakes in other businesses, but its strategic investments

(Continue on page 2)

are in three SET-listed companies: Bangkok Expressway and Metro PLC (BEM), TTW PLC (TTW), and CK Power PLC (CKP). These three firms provide products that meet basic needs (i.e., transportation infrastructure and utilities) under concession contracts or long-term utility purchase contracts. CK expects to earn dividends on a recurring basis from its strategic investments. On top of dividends, these companies provide CK with sizable construction projects as they expand.

Conversely, the ratings are partially offset by the cyclical nature of the E&C industry and the stiff competition among contractors. Most projects are awarded through competitive biddings, which squeeze the profit margins of the contractors. Given a weak private-sector investment, CK is more focused on government-sponsored infrastructure projects. The government has a clear policy to launch several mega-projects as part of an economic rejuvenation campaign. However, delays in bidding and contract awards remain and are beyond the control of the contractors.

The ratings are also constrained by CK's high financial leverage. At the end of 2016, CK's debt to capitalization ratio was 72.4%, constant from 2015. CK's debt to capitalization ratio is expected to stay below 65% after mid-2017 when the MRT Purple Line contract 4 is completed. Nevertheless, the debt to capitalization ratio is expected to remain elevated, taking into consideration the working capital needs and the sponsor loan. As of December 2016, the Xayaburi project drew down loan amounting Bt10.1 billion. The ratio of funds from operations (FFO) to total debt was low at 2.6% as of December 2016. TRIS Rating considers CK's leverage level to be higher than those of other contractors with the same ratings. However, the leverage level is consistent with CK's credit ratings in light of the company's business model as a contractor and an investment company.

TRIS Rating's base-case scenario expects CK to generate a revenue range of Bt38-Bt42 billion per annum during 2017-2019. The revenue from the Xayaburi project is expected at Bt7-Bt9 billion per annum, or 15%-20% of the base-case revenue. In addition, CK's strong backlog will secure about 80% of the base-case revenue in 2017, 50% in 2018, and 35% in 2019. CK's operating margin (operating income before depreciation and amortization, as a percentage of revenue) during 2017-2019 will stay above 6% on average. FFO should be at least Bt2.7 billion per annum.

CK's liquidity profile is acceptable. The company had Bt11.4 billion in cash plus current investments of Bt1.1 billion at the end of 2016. The debts due over the next 12 months are around Bt6.6 billion. The liquidity profile is enhanced by the company's financial flexibility through its investments in the three SET-listed companies. At the end of 2016, the fair value of CK's investments in the SET-listed companies was Bt50.3 billion, or about 88% of the company's total debt. During 2017-2019, the EBITDA (earnings before interest, tax, depreciation, and amortization) interest coverage ratio is expected to stay above 3 times. The FFO to total debt ratio is expected to range from 6%-8%.

CH. Karnchang PLC (CK)

Company Rating:

A-

Issue Ratings:

CK187A: Bt1,000 million senior unsecured debentures due 2018	A-
CK188A: Bt1,000 million senior unsecured debentures due 2018	A-
CK193B: Bt1,500 million senior unsecured debentures due 2019	A-
CK197A: Bt2,500 million senior unsecured debentures due 2019	A-
CK198A: Bt500 million senior unsecured debentures due 2019	A-
CK213A: Bt4,000 million senior unsecured debentures due 2021	A-
CK228A: Bt3,000 million senior unsecured debentures due 2022	A-
CK233A: Bt4,000 million senior unsecured debentures due 2023	A-
CK247A: Bt1,500 million senior unsecured debentures due 2024	A-
CK267A: Bt2,700 million senior unsecured debentures due 2026	A-
CK283A: Bt800 million senior unsecured debentures due 2028	A-
Up to Bt6,000 million senior unsecured debentures due within 12 years	A-
Rating Outlook:	Stable

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