TRIS RATING
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EAST COAST FURNITECH PLC

No. 89/2024
31 May 2024

CORPORATES

Company Rating:	B
Outlook:	Negative

Last Review Date: 09/04/24

Company Rating History:

Date	Rating	Outlook/Alert
09/04/24	B+	Alert Negative
19/07/23	BB-	Stable
27/07/22	BB	Stable
30/07/21	BB+	Stable
23/07/20	BB+	Negative
25/07/18	BB+	Stable
19/06/17	BB	Stable

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RATIONALE

TRIS Rating downgrades the company rating on East Coast Furnitech PLC (ECF) to "B" from "B+". The rating outlook is "negative". At the same time, we remove the CreditAlert with a "negative" implication placed on ECF's rating since 9 April 2024, as the company has successfully managed the key refinancing risk of debentures maturing in May and June 2024.

The rating downgrade reflects ECF's continued weak profitability reported for the first quarter of 2024 and uncertainty over the company's ability to restore its profit margin to levels seen before the 2023 fire incident. The "negative" outlook reflects an expected rise in debt level as the company is unlikely to be able to generate enough cash flow to cover interest expenses in the coming quarters. Unless ECF can sufficiently monetize its investment in the Minbu Solar Power Project and source the funding needed to replace damaged machinery, a further downgrade is likely.

The "B" rating reflects the company's very tight liquidity with high financial leverage which is the result of weak cash flow in the furniture business, high working capital needs, and continuing delay in the Minbu Project.

KEY RATING CONSIDERATIONS

Weakened cash flow and debt servicing capability

ECF's profitability and earnings have dropped significantly since a fire damaged the company's production facilities in the second quarter of 2023. The losses of some automated machines have led to reduced productivity coupled with an increase in overtime payments and other expenses. The margin of its earnings before interest, taxes, depreciation, and amortization (EBITDA) improved to 6.7% in the first quarter of 2024, up from 3.0% in 2023, but remained significantly below the normal range of 13%-15% prior to the fire. The weakened cash flow has also impacted the company's interest serviceability, with EBITDA falling to THB26 million in the first quarter of 2024, while interest payments amounting to THB46 million during the same period.

Without a substantial improvement in productivity, ECF's debt servicing challenge is likely to continue, causing downward pressure on the credit rating. The company is in the process of ordering new machines and seeking support from financial institutions. According to the company, machine replacement is expected to be completed in the third quarter of 2024. However, there remains some uncertainty over the company's ability to secure adequate financing. In addition, the extent of margin improvement post-installation still needs to be monitored. In the meantime, ECF's profitability could partially recover with work shift adjustments aimed at reducing overtime costs.

Weak exports offset by domestic sales

ECF's strategic refocus on accelerating domestic sales is likely to help sustain its overall revenue. Furniture exports have dropped for two consecutive years, particularly to the US and Japanese markets. However, this drop has largely been offset by its escalating domestic sales, resulting in a 2.5% drop in overall furniture revenue in 2023. However, the focus on domestic sales may lead to potential risks associated with the quality of accounts receivable, as experienced in the past, since part of the additional domestic revenue is derived from dealers.

In the first quarter of 2024, ECF's overall furniture revenue rose by 19.1% while domestic growth momentum continued with a sales increase of 28% year-on-year (y-o-y). Export sales also showed signs of recovery, reporting a 9.6% y-o-y growth.

Cash flow tied up with working capital and non-productive spending

ECF's cash has also been drained by its extensive working capital needs, resulting from high levels of accounts receivable and inventory. The average days of accounts receivable and inventory remain high at around 130-155 days and 350-400 days, respectively. The company is currently negotiating improved credit terms with both customers and suppliers to alleviate the liquidity squeeze.

The company's cash flow is also tied up in several non-productive investments including a THB100-million deposit for a Japanese biomass power plant feasibility study and a THB30-million deposit for land for durian plantation.

Continuing delay in the Minbu Project

ECF's execution risk in the Minbu Project, a 220-megawatt (MW) solar power project in Myanmar, remains high due to inadequate financing to proceed with subsequent phases. The project is still being assessed by a Chinese lender and insurer. Owing to the elevated country risk in Myanmar, the current lender has limited its funding, agreeing to provide project loans for the construction of phase 2 and phase 3 only, but leaving phase 4 with insufficient financing. As a result, the project has stalled, with only phase 1 completed.

In our view, the project development is likely to be delayed further. ECF holds a 20% interest in the Minbu Project with total exposure of THB999 million as of the end of March 2024, including a THB72.5-million shareholder loan. The project contributed shared profit of THB9.1 million in the first quarter of 2024. However, no significant dividends have been paid as yet.

Financial leverage expected to remain elevated

During 2024-2026, we expect the company's revenue to grow to THB1.5-THB1.7 billion per year. EBITDA is expected to gradually recover, increasing to THB110 million in 2024 and THB160 million in 2026. We have not incorporated the full potential for cash flow recovery as there remains uncertainty as to when the planned machine replacement will be completed. The company's interest payments will likely be in the THB185-THB200 million per annum range.

We project ECF's capital expenditure of THB90-THB120 million per annum over the forecast period. As a result, we expect a net debt to EBITDA ratio to exceed 15 times and the ratio of funds from operations (FFO) to net debt will stay in a negative territory. We expect the company to maintain a flexible capital expenditure plan in order to save cash for its business operations and debt repayment obligations.

Very tight liquidity with significant refinancing risk

We expect the company's FFO to remain negative as interest payments are likely to exceed the cash generated. ECF also faces repayments totaling THB903.8 million for debentures maturing in 2025. The company intends to divest its ownership stake in the Minbu Project with the aim of enhancing its liquidity and reducing leverage. Negotiations regarding this divestment are currently underway among the project owners and potential investors. However, in our view, the likelihood of the company receiving a large sum for its stake in the Minbu Project seems slim given the ongoing political situation in Myanmar.

ECF has successfully managed its recent refinancing needs for debentures maturing in May and June 2024. For debenture issue ECF245A, with principal repayment of THB200 million due on 11 May 2024, ECF has secured new sources of finance to settle the debenture payment. For debenture issue ECF246A of THB409.5 million, ECF has secured approval for a one-year extension of the principal repayment, postponing the repayment date from 9 June 2024 to 9 June 2025. As part of the extension, ECF is obliged to make a partial repayment of 5% of the outstanding principal amount on the original repayment date, with an increase in the interest rate from 7.15% to 7.4% per annum on the remaining principal amount. We presume the company will be able to prepare approximately THB20.5 million to cover the 5% partial payment on 9 June 2024.

Debt structure

At the end of March 2024, ECF's total outstanding debt was THB2.23 billion including priority debt of THB1.1 billion. The priority debt ratio was 49.2%. The priority debt ratio is likely to surpass 50% in the near future as the company's new borrowing to refinance the debenture issue ECF245A consists of secured debt.

BASE-CASE ASSUMPTIONS

- Revenue to rise to THB1.5 billion in 2024 and THB1.7 billion in 2026.
- Share of profits from the Minbu Project of THB30-TH35 million per annum during 2024-2026 with no dividend payments.
- EBITDA margin to gradually recover to 7% in 2024 and 10% during 2025-2026.
- Capital expenditure of THB90-THB120 million per annum during 2024-2026.
- No dividend payment.

RATING OUTLOOK

The "negative" outlook reflects the company's tendency to incur more debt as cash generation is likely to remain insufficient to cover interest expenses, at least until the company can secure the financing needed to replace damaged machinery or is able to reduce its debt burden by divesting its stake in the Minbu Project.

RATING SENSITIVITIES

A rating downgrade could occur if ECF's performance falls significantly short of our expectations. An upward revision would occur if we see a considerable improvement in ECF's financial leverage and liquidity, a scenario that would occur from successful divestment of the Minbu Project, and its profitability returns to the level recorded prior to the fire incident.

COMPANY OVERVIEW

ECF engages in the manufacture and distribution of home furniture in Thailand. The company owns two factories in Rayong Province, focusing on producing knockdown furniture and rubber wood furniture. Revenue from selling furniture contributes over 90% of its total revenue; the remainder is derived from selling decorative foil paper and dried rubber wood. ECF has been listed on the Market for Alternative Investment (MAI) since 2013.

ECF distributes its furniture products through two main channels, including made-to-order for export and Thai modern trade. Almost all made-to-order furniture is exported to leading furnishing distributors and large modern trade retailers in Japan. In Thailand, the company distributes furniture through well-known modern trade retailers, such as Home Pro, Big C, Mega Home, Thai Wasadu, Lotus's, and Global House.

The company, through ECF Power Co., Ltd., has invested in power business in the Minbu Project, a 220-MW solar power plant in Myanmar. The project consists of four phases. The first phase with 50 MW has already achieved the commercial operating date since September 2019.

KEY OPERATING PERFORMANCE

Table 1: ECF's Revenue Breakdown by Distribution Channel

Revenue (Mil. THB)	2019	2020	2021	2022	2023	Q1/23	Q1/24
Made to order (export)	706	869	950	706	554	130	143
Modern trade	372	386	472	586	591	137	174
Showroom	27	48	25	12	-	5	25
Warehouse and dealer	90	28	49	68	193	31	19
Total revenue	**1,195**	**1,331**	**1,495**	**1,372**	**1,338**	**303**	**361**
% change	*(7.9%)*	*11.3%*	*12.4%*	*(8.2%)*	*(2.5%)*		*19.1%*

Source: ECF

Table 2: ECF's Power Project Portfolio as of 30 Mar 2024

Project/Country	Type	Held by ECF (%)	Installed Capacity (MW)	Contracted Capacity (MW)	COD
Myanmar					
Minbu Project					
- Phase 1	Solar	20	50	40	Sep 2019
- Phase 2	Solar	20	50	40	Delay
- Phase 3	Solar	20	50	40	Delay
- Phase 4	Solar	20	70	50	Delay
Total			**220**	**170**	

Source: ECF

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS*

Unit: Mil. THB

	Jan-Mar 2024		---------- Year Ended 31 December ---------			
			2023	2022	2021	2020
Total operating revenues	384		1,389	1,450	1,585	1,401
Earnings before interest and taxes (EBIT)	24		15	197	188	172
Earnings before interest, taxes, depreciation, and amortization (EBITDA)	26		42	217	200	192
Funds from operations (FFO)	(21)		(142)	54	61	49
Adjusted interest expense	46		182	159	135	133
Capital expenditures	44		92	189	150	100
Total assets	4,124		4,034	3,988	3,756	3,545
Account receivables	592		568	596	454	331
Inventory	1240		1,230	1,277	1,314	1,370
Adjusted debt	2,224		2,184	2,219	1,996	1,684
Adjusted equity	1,202		1,180	1,367	1,327	1,240
Adjusted Ratios						
EBITDA margin (%)	6.7		3.0	14.9	12.6	13.7
Pretax return on permanent capital (%)	(0.4)	**	0.4	5.6	5.7	5.5
EBITDA interest coverage (times)	0.6		0.2	1.4	1.5	1.4
Debt to EBITDA (times)	198.5	**	51.8	10.2	10.0	8.8
FFO to debt (%)	(8.0)	**	(6.5)	2.4	3.0	2.9
Debt to capitalization (%)	64.9		64.9	61.9	60.1	57.6

* *Consolidated financial statements*
** *Annualized with 12 months trailing*

RELATED CRITERIA

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

East Coast Furnitech PLC (ECF)

Company Rating:	B
Rating Outlook:	Negative

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