THAI POLYCONS PLC

No. 192/2024
28 October 2024

CORPORATES

Company Rating: BB+
Outlook: Stable

Last Review Date: 25/10/23

Company Rating History:

Date	Rating	Outlook/Alert
25/10/23	BBB-	Negative
29/10/21	BBB-	Stable
09/10/18	BBB	Stable

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RATIONALE

TRIS Rating downgrades the company rating on Thai Polycons PLC (TPOLY) to “BB+” from “BBB-”. At the same time, we revise the rating outlook to “stable” from “negative”. The downgrade reflects the prolonged earnings weakness of TPOLY’s construction business amidst sluggish market conditions, making the group’s credit metrics remain incommensurate with the previously assigned rating. The rating downgrade also considers the company’s escalating liquidity pressure.

The rating factors in the reliable cash generation from the group’s power business, which has considerably helped offset its ailing construction business. However, the strengths of the power business are held back by vulnerability to feedstock supply risk and volatile prices, as well as the risks associated with overseas investments. TPOLY’s mediocre competitive position and weak profitability in the construction business remain the key rating constraints.

KEY RATING CONSIDERATIONS

Eroding construction results

We view TPOLY’s construction business as remaining a drag on the group’s overall earnings. The company’s earnings recently missed our estimate as its construction business continued to incur losses. Although the power business continues to be the group’s profit center, the construction business has hindered its overall performance. The construction business has significantly accounted for about half of the group’s revenue.

TPOLY severely suffered from a surge in raw material prices following the Russia-Ukraine conflict. The fixed price construction contracts, but inflated costs, resulted in cost overruns on some of the projects undertaken during 2020-2022. TPOLY also endured adverse impacts from cost evaluation, insufficient labor, and underperforming subcontractors. The construction business incurred net losses of THB393.7 million in 2023 and THB90.5 million in the first half of 2024. In contrast, the power business earned THB441.9 million in profit in 2023 and THB260.4 million in the first half of 2024. Apart from the weak results, TPOLY has experienced long overdue payments by some of its construction clients.

Looking forward, we expect the construction business to recover, as most of the troubled projects are scheduled to be completed in the next two years. In our base-case projection, we assume the gross margin of the construction business will turn positive, staying in the 4%-6% range, during 2025-2026 from negative in 2024. Nevertheless, such levels of gross margin will unlikely be sufficient to make the construction business profitable. Also, we view the sluggish construction market conditions and intense competition to remain a hindrance to earnings improvement.

Mediocre competitiveness in construction business

We view TPOLY as having mediocre competitiveness in the construction business. The company carries a narrow scope of construction work, concentrating on the construction of buildings, such as hospitals, universities, hotels, and shopping malls. TPOLY generally undertakes construction work worth below THB1 billion per contract. The company has a revenue base of about THB2 billion per annum, relatively smaller compared with other rated construction companies.

The small business scale and the narrow scope of work limit bargaining power and business opportunities, and hence competitiveness. With the intense market competition, the company's construction business typically yields thin profit margins. Any interruptions on its work could readily translate into cost overruns.

In the first nine months of 2024, TPOLY acquired new construction contracts worth about THB1.6 billion in aggregate, significantly increasing from a low of THB319 million in 2023. The company recently reduced the number of its permanent construction workers to lessen fixed expenses. The more flexible cost structure should reduce the pressure to undertake low-margin construction works.

Reliable cash flows from power business

The rating on TPOLY is supported by reliable cash flows from its power business, representing the company's entire consolidated EBITDA during the past five years. The group's power business is carried out by the core and profit-making subsidiary, TPC Power Holding PLC (TPCH). Currently, TPCH owns 11 power projects including biomass, waste-to-energy (WTE), and a solar farm. We expect the aggregate contracted capacity of the operating plants to increase to 362 megawatts (MW) in 2026 from 81.8 MW in 2024.

The reliability of cash flows is aided by multi-year power purchase agreements (PPAs) with credible state-owned producers and distributors of electricity. The operating power plants have delivered satisfactory results with an average capacity factor of 80%-90% over the past several years. The bulk of earnings from the power business is crucial in our assessment of TPOLY's credit profile, counteracting the weak earnings of the construction business.

Vulnerability to feedstock risk

The power business is highly vulnerable to feedstock supply risk. The availability of feedstock relies on several factors, such as seasonality, use of biomass in other industries, and number of biomass power plants. In securing sufficient feedstock, TPCH holds long-term supply agreements with local suppliers. Nonetheless, contract enforcement is virtually challenging.

Also, earnings of biomass power plants are exposed to the volatile prices of feedstock. Biomass fuel prices can swing wildly while feedstock varies in terms of humidity and calorific value. As for WTE, different types of waste provide different calorific value, while contaminants can affect operational stability.

Overseas investment risks

TPCH has strategically expanded the power portfolio into the Lao People's Democratic Republic (Lao PDR) and Cambodia, leading to meaningful exposure to higher country and regulatory risks. TPCH has invested in a 40% stake in Laos-based Maekhong Power Co., Ltd. (MKP), the project company developing a 100-MW solar farm to sell electricity to Electricite du Laos (EDL) under a 25-year PPA. The project is slated to start commercial run in 2025, receiving a fixed tariff rate over the PPA life, and is part of the PPA between EDL and Electricity of Cambodia (EDC). This implies that EDC will be the indirect off-taker of the project. Hence, the market risk is somewhat mitigated. Nevertheless, the counterparty of MKP is still EDL. The weakened credit profile of EDL increases the counterparty risk to TPCH.

Additionally, TPCH is jointly developing other renewable power projects with its partner, including a 180-MW solar farm in Cambodia, currently under permit approval processes. TPCH has already spent THB383 million in this project.

We view the credit profiles of the state-run EDL and EDC, the purchasers of electricity, as not as strong as the state-owned power buyers in Thailand. Also, TPCH will be at risk of the cross-border risks of fund transferability and currency convertibility with respect to the dividend income it will receive from the investment projects. We consider investments with higher country and regulatory risks as increasing the group's business risk. As such, we expect the new investments will bring in returns commensurate with their respective risks.

Operating performance to improve

As the sponsor for power projects, TPCH has provided guarantees on the debt obligations of some joint ventures (JVs) in proportion to its stakes in the JVs. Given the financial ties to the JVs, we include the assets, liabilities, and respective financial performances of the JVs in the group's consolidated accounts, in proportion to the ownership in each venture, to better reflect the group's financial risk profile.

We view improvement in the group's earnings over the next three years as highly hinging on recovery in the construction business. Assuming new construction contracts worth THB1-THB2 billion annually, we forecast revenue from the construction business will be THB1-THB2 billion per annum during 2024-2026. The power business should continue to perform satisfactorily, generating an annual revenue of THB2.5-THB2.6 billion. As a result, TPOLY's total operating revenue should range between THB3.7-THB4.6 billion per annum. We anticipate its annual EBITDA to be THB850-THB900 million in the years ahead, with an EBITDA margin of 20%-23%.

However, we view turnaround in the construction business to remain fragile, given the sluggish prospect of domestic construction activities and stiff competition.

Credit metrics to remain weak

TPOLY's financial leverage recently improved, with a debt to EBITDA ratio lowering to 7 times (annualized with trailing 12 months) in the first half of 2024, from a peak of about 12 times during 2021-2022. This followed improvement in the power business' performance, plus the recent divestment of five biomass power projects that brought in THB1.4 billion in cash and helped reduce debt burdens. Nevertheless, we project the consolidated debt to EBITDA ratio will be sustained at 7 times over the next three years, the level incommensurate with the previously assigned rating.

In our base-case projection, the power business will likely push TPCH's debt loads, following the committed investments. In addition to the power projects abroad, TPCH has two WTE projects in Thailand in the pipeline. The projects are being developed by subsidiaries of Siam Power Co., Ltd. (SP). As TPCH is the major shareholder of SP, we assume TPCH will provide guarantee for the respective project loans, the same financing structure as the first WTE. Therefore, we proportionately add outlays with respect to the new WTEs to the group's planned investments. In contrast, we assume TPCH's overseas projects will be able to seek project loans, without the requirements of sponsor guarantees or additional financial support by TPCH.

The power portfolio expansion will likely need THB2 billion in investment spending during 2024-2026. The construction business is, in contrast, forecast to require less debt, given the earnings recovery expectation. We also expect TPOLY to successfully improve its working capital management for the construction business, particularly the long overdue accounts receivable. As a result, we predict the company's gearing will stay at the current level, with the debt to EBITDA ratio of about 7 times during 2024-2026. The fund from operation (FFO) to debt ratio should hover around 8% and the debt to capitalization ratio stay at about 65%. We note that the group's financial risk profile could change if the project loans for its JVs could be structured to prevent the creditors having recourse to the group.

Heightening liquidity pressure

The rating considers escalating pressure on the group's liquidity. Excluding the debt of JVs guaranteed by TPCH, the group had consolidated short-term loans and long-term debt obligations of THB2.4 billion coming due in the next 12 months from June 2024. Taking into account sources of funds (e.g. cash on hand, estimated FFO, and undrawn credit facilities) and its committed investment plan, we assess the group will have to rollover its short-term working capital loans and refinance substantial amounts of maturing long-term debt. We also expect a potential liquidity shortfall. TPOLY's other sources of funds (e.g. land disposal and partial divestments of its stake in SP) should help support liquidity if materialized.

Debt structure

In assessing the level of the group's priority debt, we exclude the debt incurred by the JVs which is guaranteed by TPCH. As such, TPOLY's consolidated debt was THB5.5 billion as of June 2024. Of this, almost all was considered priority debt, comprising TPOLY's secured debt and all borrowings incurred by its subsidiaries. As a result, we view the company's unsecured creditors as being significantly disadvantaged to its priority debt holders with respect to claims against the company's assets.

BASE-CASE ASSUMPTIONS

Key assumptions in TRIS Rating's base-case forecast during 2024-2026 are as follows:

- Aggregate contracted capacity of operating power plants to be 362 MW in the next three years.
- Average capacity factor of operating power plants to range between 80%-90%.
- New contracts for construction work to be worth THB1-THB2 billion annually.
- Total operating revenue to be THB3.7-THB4.6 billion per annum.
- EBITDA margin to stay in 20%-23% range.
- Capital expenditures and investments to total THB2 billion.

RATING OUTLOOK

The "stable" outlook reflects our expectation that TPOLY's operating performance will gradually recover. The construction business should turn around as forecast, while the power business will remain the core profit generator, delivering satisfactory results. We also expect TPOLY to prudently manage its liquidity.

RATING SENSITIVITIES

We are unlikely to raise the rating on TPOLY in the near term. However, we could consider an upgrade if TPOLY's credit metrics improve significantly. This could occur from a profitability improvement in the construction business, or a material reduction in debt obligations. An upgrade scenario also requires a healthier liquidity position.

We could downgrade the rating on TPOLY if its business and financial profiles deteriorate further. This could develop from a prolonged weak performance of the construction business, or more aggressive debt-financed investments than our estimates, or materially enhanced exposures carrying high country and regulatory risks. Negative pressure on the rating could also emerge from a worsening liquidity position.

COMPANY OVERVIEW

Established in 1988, TPOLY is a construction contractor providing engineering and construction (E&C) services to the public and private sectors. The company focuses on constructing buildings and civil works. The company was listed on the Market for Alternative Investment (MAI) in 2009 before switching to the Stock Exchange of Thailand (SET) in 2010. TPOLY expanded into the residential property and the power businesses in 2010. It spun off the power business to TPCH, its subsidiary, in 2012. The Chanpalangsri Family remained the major shareholder, holding an approximate 44% interest in TPOLY, as of March 2024.

The construction business made up about half of TPOLY's total revenue. However, the power business accounted for all TPOLY's earnings. As of September 2024, TPOLY's power portfolio had an aggregate contracted capacity of 197.8 MW, across seven biomass power projects (73.8 MW), three WTE projects (24 MW), and one solar power project (100 MW). Eight of its power plants are currently operating (81.8 MW).

KEY OPERATING PERFORMANCE

Table 1: Revenue Breakdown

Unit: %

Segment	2020	2021	2022	2023	Jan-Jun 2024
Construction	55	43	47	51	27
Property	1	0	0	-	
Power	45	57	53	48	71
Trading	0	0	0	1	2
Total	**100**	**100**	**100**	**100**	**100**
Total revenue (mil. THB)	**3,974**	**4,344**	**5,029**	**6,001**	**1,664**

Source: TPOLY

Table 2: Power Project Portfolio (as of Sep 2024)

Company/Country	Held by TPCH (%)	Status	Installed Capacity (MW)	Contracted Capacity (MW)	Tariff
Biomass Projects					
CRB	73	Operating	9.5	9.2	FiT
MWE	85	Operating	9.0	8.0	FiT
MGP	46	Operating	9.5	8.0	FiT
TSG	65	Operating	9.5	9.2	FiT
PGP	60	Operating	9.9	9.2	FiT
SGP	51	Operating	9.9	9.2	FiT
PTG	95	Operating	23.0	21.0	Adder
Sub total - Biomass			**80.3**	**73.8**	
Waste Projects					
SP	50	Operating	9.5	8.0	FiT
SPNS	45	Developing	9.9	8.0	FiT
SPNK	40	Developing	9.9	8.0	FiT
Sub total - Waste			**29.3**	**24.0**	
Solar Projects					
MKP	40	Developing	130.0	100.0	Fixed Rate
Sub total - Solar			**130.0**	**100.0**	
Grand total			**239.6**	**197.8**	

Source: TPCH

CRB = Chang Raek Bio Power
MGP = Mahachai Green Power
PGP = Phathalung Green Power
PTG = Pattani Green
SPNS = Siam Power Nongsarai
MKP = Maekhong Power
MWE = Maewong Energy
TSG = Thungsung Green
SGP = Satun Green Power
SP = Siam Power
SPNK = Siam Power Naklang

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS*

Unit: Mil. THB

		------------Year Ended 31 December ---------			
	Jan-Jun 2024	**2023**	**2022**	**2021**	**2020**
Total operating revenues	1,814	6,264	5,312	4,391	3,906
Earnings before interest and taxes (EBIT)	342	385	217	95	448
Earnings before interest, taxes, depreciation, and amortization (EBITDA)	492	820	602	481	704
Funds from operations (FFO)	304	424	289	275	581
Adjusted interest expense	176	383	296	194	123
Capital expenditures	103	282	423	504	1,428
Total assets	10,773	10,948	12,577	11,997	10,903
Adjusted debt	5,644	5,642	6,955	5,676	4,673
Adjusted equity	3,219	3,329	3,669	3,803	4,448
Adjusted Ratios					
EBITDA margin (%)	27.1	13.1	11.3	11.0	18.0
Pretax return on permanent capital (%)	4.3 **	3.8	2.0	1.0	5.1
EBITDA interest coverage (times)	2.8	2.1	2.0	2.5	5.7
Debt to EBITDA (times)	7.0 **	6.9	11.6	11.8	6.6
FFO to debt (%)	7.2 **	7.5	4.2	4.8	12.4
Debt to capitalization (%)	63.7	62.9	65.5	59.9	51.2

Note: *The figures include assets, liabilities, and the respective financial performances of Mahachai Green Power Co., Ltd. (MGP) and Siam Power Co., Ltd. (SP), in proportion to the ownership stake in these JVs.*

* *Consolidated financial statements*

** *Adjusted with trailing 12 months*

RELATED CRITERIA

- Group Rating Methodology, 7 September 2022
- Corporate Rating Methodology, 15 July 2022
- Key Financial Ratios and Adjustments for Corporate Issuers, 11 January 2022
- Issue Rating Criteria, 15 June 2021

Thai Polycons PLC (TPOLY)

Company Rating:	BB+
Rating Outlook:	Stable

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