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TTCL PLC

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Company Rating: BBB

Outlook: Stable

Company Rating History:

Date	Rating	Outlook/Alert
28/03/14	BBB+	Stable

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Rating Rationale

TRIS Rating downgrades the company rating of TTCL PLC (TTCL) to “BBB” from “BBB+”. The downgrade reflects TTCL’s weakened operating performance following a precipitous falloff in new contracts signed as well as higher-than-expected leverage.

The rating continues to reflect TTCL’s strengths in EPC (engineering, procurement, and construction) for the industrial segment, its capability to undertake larger projects in Thailand and abroad, as well as its strategic diversification into the power business. However, these strengths are partially offset by heightened leverage, operating risks of projects abroad, cyclicality of the EPC industry, and severe competition.

TTCL was established in 1985 as a joint venture between Italian-Thai Development PLC (ITD) and Toyo Engineering Corporation (TEC), a Japanese EPC firm. TTCL was listed on the Stock Exchange of Thailand (SET) in 2009. As of August 2017, TEC was the major shareholder of TTCL, holding 10% of the company’s shares. TTCL is positioned as an integrated EPC contractor for industrial plants including refineries and plants which produce petrochemicals, chemicals, fertilizer, oil and gas, and electrical power.

TTCL has moved to undertake larger projects and grow its footprint abroad. Despite the concentration risk stemming from large projects, the company’s track record of project execution and quality performance is substantiated by a list of creditworthy customers, including large refining and petrochemical companies. The company has also expanded and become a producer of electrical power, a move aimed at offsetting the cyclicality and stiff competition in the EPC industry. As a result, the move has led to a more debt-heavy financial structure.

The rating downgrade is built on TTCL’s weaker-than-expected operating performance. Given its end markets served, TTCL is strongly impacted by sluggish investment in the private sector. Revenue in the first nine months of 2017 devastatingly dropped by 46% year-on-year (y-o-y) to Bt8.3 billion, which was below TRIS Rating’s expectation. TTCL would arrive at Bt9-Bt10 billion in revenue in 2017 and 2018, while its revenue in the past three years hovered around Bt20 billion per annum. The drop-off in revenue is caused by a precipitous falloff in new contracts signed. TTCL’s growth has languished as its backlog starts to dissipate.

The downward rating pressure has also developed from TTCL’s weakened financial profile as its debt remains elevated. TTCL’s leverage level is much higher than TRIS Rating’s expectation, due in large part to the rising working capital needs and its additional investment in the power segment.

The current rating continues to reflect TTCL’s strengths in EPC for the industrial segment. TTCL is among the top five SET-listed contractors, in terms of revenue base and asset size. The company is capable of undertaking large EPC projects and expanding geographically. TTCL has undertaken EPC projects in several countries, including Qatar, Malaysia, and Vietnam. TTCL recently pared down its operations in the U.S., placing a greater emphasis on neighbouring countries. During 2015 through the first nine months of 2017, overseas projects made up about 60% of total revenue. Geographical diversity supports the ratings.

The rating also takes into account TTCL’s strategy to expand into the power business, a move that helps TTCL secure EPC contracts and earn a steady revenue stream. The main and largest power project in which TTCL invests is the 120-

megawatt gas-fired power plant in Ahlone, Myanmar, the “Ahlone Project”, which carries a total investment cost of about Bt5.5 billion. Despite its smaller revenue contribution, the power segment has generated a sizable amount of EBITDA (earnings before interest, taxes, depreciation, and amortization) as the Ahlone power plant comes to fruition. For the first nine months of 2017, the power segment accounted for around 68% of TTCL’s EBITDA, or Bt660 million.

Conversely, the rating is weighed down by TTCL’s weakened capital structure. TTCL borrowed more to fund its working capital needs for larger projects, undergoing a much longer cash conversion cycle. TTCL also borrowed to fund its additional investment in the power segment. The company recently engaged in acquiring a series of additional shares of TTCL Power Holdings Pte. Ltd, which cost TTCL a total of about Bt1.8 billion.

TTCL plans to invest in and build two coal-fired power plants in Myanmar, each with a production capacity of 1,280-megawatts. Each project will cost around Bt100 billion. However, TRIS Rating is of the view that the likelihood that both projects will take wing in the near term is remote, considering the size of investment and the slow-moving government bureaucracy of Myanmar. However, TTCL’s leverage will increase considerably should the deals be completed.

The rating is also partly offset by the operating risks associated with projects abroad, despite the benefits TTCL receives from geographical diversification. Failures in project execution could cause significant negative repercussions for TTCL’s performance. Moreover, TTCL has experienced severe competition, particularly in overseas projects. The competition slashed TTCL’s overall gross margin to below 10%.

TTCL is very susceptible to the cyclicality of the EPC segment. The slowdown in investment of private refining and petrochemical companies drastically dragged on its revenue and profits. TTCL could not secure new contracts in 2016. The company won Bt8 billion worth of new projects in the first nine months of 2017; however, this was less than expected, leading to a steep decline in revenue. As of September 2017, TTCL’s backlog stood at Bt13.7 billion. The total value of the current projects in the backlog will be realized 20% of TTCL’s revenue during 2017, 48% in 2018, 28% in 2019, and 10% in 2020, according to TRIS Rating’s base case.

TTCL’s financial profile for the first nine months of 2017 was lower than TRIS Rating’s expectation. The operating margin (operating profit before depreciation and amortization as a percentage of revenue) was 7.06%. Under TRIS Rating’s base-case scenario, which excludes the investment in the two coal-fired power plants in Myanmar, TTCL’s revenue in 2017 and 2018 would range around Bt9-Bt10 billion, due to fewer new projects to replenish the backlog. Revenue will range from Bt17-Bt20 billion per annum during 2019-2020, assuming resurgence in private investment.

TRIS Rating expects the operating margin will range around 7%-8% during 2018-2020. Operating income is expected to rise because the company will receive recurring income from the Ahlone project on top of construction revenue. Funds from operations (FFO), which include income and cash received from the leased assets (Ahlone power plant), would range from Bt0.5-Bt1.1 billion per annum.

During 2018-2020, TRIS Rating’s base-case scenario expects TTCL’s debt to capitalization ratio will stay between 67%-70%. Cash flow protection, as measured by the FFO to total debt ratio and the EBITDA interest coverage ratio, are expected to improve. TTCL will receive recurring income from the Ahlone project, pushing the cash flow protection measures higher. During 2018-2020, the FFO to total debt ratio is expected to stay in a range of 5%-10%, while the EBITDA interest coverage ratio will stay at 3 times or above.

Rating Outlook

The “stable” outlook reflects the expectation that TTCL will maintain its strong market position in the EPC sector. TTCL could secure sizable new contracts to replenish its backlog. The operating margin is expected to stay between 7%-8% and the total debt to capitalization ratio will not exceed 70% over the next three years. In addition, TTCL is expected to prudently manage its liquidity in order to repay the debts coming due.

A rating upgrade is unlikely in the near term but could occur if TTCL could deliver better-than-expected operating performance and its leverage falls significantly. A rating downgrade could emerge if TTCL’s operating performance falls short of the estimate while the company remains saddled with debts, with the total debt to capitalization ratio exceeding 70% for a sustained period.

TTCL PLC (TTCL)

Company Rating:	BBB
Rating Outlook:	Stable

Financial Statistics and Key Financial Ratios *

Unit: Bt million

	Jan-Sep 2017	------------------------ Year Ended 31December -------------------- 2016	2015	2014	2013	2012
Revenue	8,294	20,024	21,524	19,575	17,865	11,358
Finance cost	323	428	355	106	27	0
Net income from operations	72	355	137	506	775	482
Funds from operations (FFO)	(410)	666	1,200	414	825	520
Adjusted funds from operations (Adjusted FFO)	275	1,072	1,372	533	825	520
Capital expenditures	115	77	97	56	81	802
Total assets	25,656	25,812	25,897	22,652	14,979	7,659
Total debts	11,779	8,725	9,684	7,391	934	0
Total liabilities	20,347	19,471	19,608	16,237	9,042	5,338
Shareholders' equity	5,309	6,341	6,289	6,415	5,937	2,321
Depreciation & Amortization	38	51	49	49	30	24
Dividends	123	280	297	392	355	216
Operating income before depreciation and amortization as a % of sales	7.06	4.59	3.66	2.38	5.57	5.48
Pretax return on permanent capital (%)	3.63 **	5.94	5.32	6.33	22.96	33.50
Earnings before interest, tax, depreciation, and amortization (EBITDA) interest coverage (times)	2.99	2.82	2.37	6.64	39.65	> 40
FFO/total debt (%)	3.53 **	12.28	14.16	7.21	88.32	> 250
Total debt to capitalization (%)	68.93	57.91	60.63	53.54	13.59	0

Note: Funds from operations (FFO) are adjusted by financial assets under concession arrangement of Ahlone power plant project thus all financial ratios from 2014 onward are adjusted.

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

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