ENERGY EARTH PLC

No. 56/2017 5 June 2017

Company Rating: BBB-

Outlook: Stable

Company Rating History:

Date	Rating	Outlook/Alert
30/06/16	BBB-	Stable

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Rating Rationale

TRIS Rating affirms the company rating of Energy Earth PLC (EARTH) at "BBB-". The rating reflects EARTH's established position in the coal trade in Thailand and the moderate diversity of its markets. The rating also incorporates the company's strategy to secure a supply of coal and enhance its cost competitiveness by using prepayments and by acquiring mines in Indonesia. The strengths are partially offset by the inherent volatility in earnings, intense competition, limited track record of operating coal mines, the exposure to adverse regulatory changes in Indonesia and China, and high need for working capital which has led to a highly leveraged balance sheet.

EARTH is a medium sized coal trader in Thailand. The Phihakendr and Khamdee families founded Energy Perfect Co., Ltd. (EPCL) in 2007, and made a reverse takeover (backdoor listing) of Advance Paint and Chemical (Thailand) PLC in 2010. Since then, the company was renamed Energy Earth PLC, and EPCL has become EARTH's subsidiary. EARTH was initially listed on the Market for Alternative Investment (MAI) in 2010. The company applied for a dual listing on the Frankfurt Stock Exchange in 2013 before moving from MAI to be listed on the Stock Exchange of Thailand (SET) in 2014. As of May 2017, the Phihakendr and Kamdee families were the major shareholders, holding approximately a 29% interest in EARTH.

Since its establishment in 2007, EARTH's sales volume and customer base have continued to grow. Sales volume increased from 2 million tonnes in 2011 to 12.6 million tonnes in 2016, a compound annual growth rate (CAGR) of 44%. The increase in sales volume reflected the company's ability to deliver coal on time at competitive prices. Currently, EARTH's major markets are China, Thailand, South Korea, and India. China remains the largest market, accounting for 71% of total sales in 2016, followed by Thailand and Korea, which contributed around 22% and 4%, respectively. Most of EARTH's international sales have been to coal-fired power plants. In contrast, sales to cement plants comprise around one-third of domestic (within Thailand) sales, or 8% of the total sales in 2016.

EARTH sources the majority of the coal it sells directly from miners in Indonesia, using prepayments or offtake agreements to get discounts from the miners. Prepayment to coal miners, made as advance payments and offtake agreements, amounted to Bt16,069 million as of March 2017. EARTH has a policy to own its own mines in order to secure the supply of coal and enhance its cost competency. EARTH acquired an Indonesian mining company in 2011. The acquired company runs two mines in South Kalimantan with coal reserves of 7.4 million tonnes. The extraction of coal seam was gradually completed by EARTH in 2014. Later, the company made additional acquisition of the exclusive coal offtake and purchased another Indonesian mining company totaling US$238 million (or Bt8,395 million at Bt35.24/US$). As of March 2017, EARTH's coal reserves from the two mines amounted to approximately 83 million tonnes.

Higher leverage depressed EARTH's financial profile in 2016. Profitability improved slightly as coal prices recovered, but profitability remained below historical level. Although the operating margin (operating income before depreciation and amortization as a percentage of sales) increased modestly to 10.5% in 2016, from 9.7% in 2015, but the level in 2016 was lower than operating margin of 14%-20% achieved during 2012-2014. The operating margin was lower due to absence of high margin from its own mines. The commercial operation of EARTH's own mines were delayed due to the volatility of coal prices during the past several months. EARTH's earnings before interest, tax, depreciation, and amortization (EBITDA) rose to Bt1,953 million in 2016, compared with Bt1,637 million in 2015. EBITDA rose to Bt725 million in the first quarter of 2017, a 74.1% increase from the same period of the prior year on the back of higher sales volume. However, EARTH made more advance payments and offtake agreements to support its sales growth. As a result, EARTH's debt increased from Bt17,888 million at the end of 2015 to Bt21,547 million at the end of 2016 and Bt22,829 million at the end of March 2017. Higher interest expenses and some realized foreign exchange losses pushed down funds from operations (FFO) to Bt687 million from Bt1,122 million in 2015. The company's cash flow protection was weak because of the investments in mining assets and higher working capital needs. The FFO to total debt ratio declined from 6.3% in 2015 to 3.2% in 2016 and 3.9% (annualized, from the trailing 12 months) for the first three months of 2017. The EBITDA interest coverage ratio stood at 2.3 times in 2016 and 3 times in the first quarter of 2017, compared with 2.7 times in 2015.

Looking forward, the company's FFO is projected to improve to approximately Bt1,000-Bt1,400 million per year during 2017-2019. Sales volume is forecast to rise and production at its own lower-cost mines will gradually increase. EARTH's capital expenditures are forecast at Bt400-Bt500 million per year over the next few years. The expenditures will cover the mine development and the coal-loading jetty with some discretion to delay. The company's leverage is expected to improve, but will remain high. The FFO to total debt ratio is expected to gradually improve to a range of 7%-10%. The EBITDA interest coverage ratio will remain at around 2-3 times in 2017-2019. Liquidity is manageable. About 47% of outstanding debt, or Bt10,754 million, are trade finance loans with banks. EARTH can repay this amount with its operating cash flow. Other amounts of debt due over the next 12 months comprise bills of exchange worth Bt2,395 million and long-term loans plus bonds at around Bt1,812 million. EARTH can meet these obligations by utilizing its undrawn working capital facilities of Bt3,661 million, plus FFO of Bt1,000 million and cash on hand of Bt1,238 million at the end of March 2017. However, EARTH plans to refinance its long-term loans and bonds by issuing new bonds.

Rating Outlook

The "stable" outlook reflects TRIS Rating's expectation that EARTH will maintain its competitive position and market position in the coal trading industry. EARTH's credit upside is limited over the next 12-18 months due to its current financial profile. The downside risk could materialize if the company's performance falls short of the estimates while the debt to capitalization ratio remains high. An FFO to total debt ratio below the forecast level on an extended period would also be a negative factor for the rating.

Energy Earth PLC (EARTH)

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Rating Outlook:	Stable

Financial Statistics and Key Financial Ratios*

Unit: Bt million

		---------------------------Year Ended 31 December----------------------				
	Jan-Mar 2017	2016	2015	2014	2013	2012
Sales and service revenues	7,860	18,491	16,847	14,911	13,505	10,451
Gross interest expense	239	841	615	379	293	155
Net income from operations	272	915	800	1,209	1,291	1,343
Earnings before interest, tax, depreciation, and amortization (EBITDA)	725	1,953	1,637	2,052	2,398	2,169
Funds from operations (FFO)	472	687	1,122	1,380	1,835	1,692
Total capital expenditures and investments	1	503	574	576	4	2
Total assets	35,725	34,056	29,430	17,941	13,537	8,808
Total debt	22,829	21,547	17,888	12,004	8,508	5,193
Shareholders' equity	10,691	11,112	10,711	5,297	4,330	2,857
Operating income before depreciation And amortization as % of sales	9.20	10.50	9.67	13.72	17.67	20.54
Pretax return on permanent capital (%)	7.25 **	6.31	7.05	11.47	17.58	31.64
Earnings before interest, tax, depreciation, and amortization (EBITDA) interest coverage (times)	3.03	2.32	2.66	5.42	8.19	14.02
FFO/total debt (%)	3.88 **	3.19	6.27	11.50	21.57	32.58
Total debt/capitalization (%)	68.11	65.98	62.55	69.38	66.27	64.51

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

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