

EASTERN POWER GROUP PLC

No. 224/2022
7 December 2022

CORPORATES

Company Rating: BBB-
Outlook: Negative

Last Review Date: 30/12/21

Company Rating History:

Date	Rating	Outlook/Alert
07/12/18	BBB-	Stable
01/12/15	BBB	Stable

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RATIONALE

TRIS Rating affirms the company rating on Eastern Power Group PLC (EP) at “BBB-”. However, TRIS Rating revises the company’s rating outlook to “negative” from “stable”, to reflect the persistent uncertainties related to its wind power projects in Vietnam, particularly the further delay of the project commencement date and unsettled tariff.

The rating reflects our expectation that EP’s cash flow generation will strengthen considerably once the wind power projects are operational. The rating also recognizes EP’s strong market presence in the printing industry, and the growth prospect of its paper packaging business. Conversely, the rating is tempered by EP’s significant exposure in Vietnam, the increasingly challenging renewable power industry, and the dim outlook of the printing industry.

KEY RATING CONSIDERATIONS

Pandemic-hit wind projects face serious delays

EP’s weak cash flow is the result of the prolonged delays in the commencement of operations of its much-anticipated wind power projects in Vietnam. EP has four wind farms in Vietnam that are yet to commence operations. The net capacity is 129 megawatts (MW), when measured in proportion to EP’s equity stakes in the assets. We previously expected that all of these projects would start commercial runs by the first half of 2022. As a result, EP’s earnings fell markedly short of our forecast. For the first nine months of 2022, EP’s revenue came to THB0.6 billion, far below our full-year forecast of THB1.7 billion.

Like those of many developers, EP’s wind power projects were severely affected by the Coronavirus Disease 2019 (COVID-19) pandemic. The projects encountered supply-chain bottlenecks for major components, labor mobility difficulties, and other issues at the height of the pandemic, causing them to fail to complete construction ahead of the expiry of the feed-in tariff (FIT) in November 2021.

As of October 2022, construction was mostly complete and the wind plants were ready for power commissioning. The construction of EP’s two wind projects in Quang Tri province (79 MW) was completed. The other two wind projects in Gia Lai province (50 MW) were more than 90% completed and the key equipment had been successfully installed and tested.

Pending commercial operations due to unsettled tariff

Commercial operations of the pandemic-hit projects have been pending on a new FIT. The Vietnamese government is currently resolving the FIT issues. The Ministry of Industry and Trade (MOIT) of Vietnam recently issued a circular, which sets out formulae for Vietnam Electricity (EVN) to calculate the FIT for the pending projects. EVN is responsible for collecting feasibility studies submitted by the project developers. EVN will then come up with a proposed tariff range, which will ultimately be approved by the MOIT.

We view this as a positive sign for EP’s wind power projects. However, uncertainties remain as to when the projects will eventually start commercial runs and at what tariff the electricity will be sold to EVN. In our base case, we assume the new FIT will be finalized in March 2023 while EP’s projects will commence operations in the second quarter of 2023, with a lower FIT. In our view, EP’s financial risk will be further heightened if the Vietnamese government’s final decision on FIT is delayed.

Expected sizeable earnings ahead

Over the past few years, EP has been undertaking a major power portfolio shake-up, a move aimed at strengthening its cash generation and capital structure. EP sold off its solar power projects during 2019-2020. These included solar power projects in Vietnam, Japan, and Thailand. EP also divested its interests in two cogeneration power plants in 2021. EP has primarily utilized the proceeds from the divestiture to invest in the wind power projects. With the ongoing delay, EP's revenue from the power business is currently derived from a small cluster of solar rooftop projects and solar rooftop construction works, which bring in revenues of about THB80-THB100 million per year. EP's future earnings largely hinge on the success of the wind power projects.

We expect EP's wind farms will generate sizable earnings once they are in operation. In our base case, we expect all projects to commence operation in the second quarter of 2023. We assume a tariff of US\$7.38 cents per kilowatt-hour (kWh), as opposed to the original level of US\$8.5 cents per kWh. We assume the power output will reach P90 level (the 90% probability of energy production). With these assumptions, we expect EP's revenue to recover to THB1.6 billion in 2023. Revenue is projected to grow to THB2 billion per year in 2024-2025 when all the wind projects have achieved full-year operations. We forecast earnings before interest, taxes, depreciation, and amortization (EBITDA) to be THB0.8 billion in 2023 and around THB1.1 billion per year in 2024-2025.

We expect the debt to EBITDA ratio to decline sharply to about 5 times by 2023, from 12 times in 2022. The ratio will likely stay at about 3 times in 2024-2025. At the same time, we project funds from operations (FFO) of THB0.5 billion in 2023 and around THB0.7-THB0.8 billion a year in 2024-2025. The FFO to debt ratio could increase to over 10% in 2023 and surpass 20% in 2024. We also expect EP to keep the debt to capitalization ratio in the 30%-40% range over the forecast period.

Uncertainties related to the projects remain

We place a "negative" outlook on the company rating as the forecast earnings from the wind farms remain susceptible to uncertainties. Notwithstanding the Vietnamese government's current effort to resolve the FiT issues, further delay on the resolution or the commencement of operations would pose a serious threat to EP's earnings recovery. Moreover, cash flow from the projects could be curtailed if the actual tariff is significantly lower than expected. In addition, wind power generation generally entails higher operational risks, such as mechanical and electrical breakdowns. The success of a wind power project largely hinges on the availability and speed of wind. The performances of EP's wind farms will need to be proven.

Increasingly challenging power industry

We see growth opportunities for renewable power in Thailand, with the anticipated opening of a new quota for purchases of electricity from renewable energy sources. However, competition in the domestic power market has intensified in recent years. Private companies, ranging from very small entrepreneurs to large conglomerates, have branched into the power market. Thai power companies are leaning towards expanding investments outside Thailand. Despite more growth opportunities, some overseas expansions entail higher risks, such as transparency and consistency of regulations, the credit profiles of off-takers, and environmental challenges. We also see increasing competition with a tendency towards lower tariffs in countries that have attracted large inflows of foreign investment in power generation.

Substantial exposure in Vietnam

Currently, power projects in Vietnam make up about 95% of the company's total capacity. Vietnam has offered huge opportunities for investment in renewable energy over the past years. The country is rich in natural resources to support the ongoing growth of renewable energy, aided by its long coastline, strong wind speeds, and long sunshine hours. With vigorous demand for electricity, we expect EP will further expand in Vietnam, or invest in power projects in the neighboring countries and sell the electricity to EVN.

On the other hand, investments in power projects in Vietnam currently face uncertainties, resulting from pending clarity of the country's National Power Development Plan and policies with respect to the new pricing framework for renewable energy. We also view the credit profile of the state-run EVN to be less robust than the Thai state-owned power buyers. Besides, power output from plants in Vietnam is at risk of being curtailed due to insufficient grid capacity. That said, we believe the curtailment risk will subside as the Vietnamese government improves the country's infrastructure in support of growing electricity demand.

Strong market presence in the printing business

In the printing business, EP's strong market presence is underpinned by its broad range of products, well-established track record, and long-term relationships with its customers. Despite disruption in the printing and publishing industries, EP's printing business remains profitable. However, gross profit margin in the first nine months of 2022 decreased to 10% from 14% year-on-year (y-o-y), due to higher material costs and supply chain constraints.

Small contribution from printing and packaging businesses

The printing business was EP's core revenue contributor in the past. However, the industry has been disrupted by the growth of digital media, which has resulted in subdued demand for printing services. The value of print advertising has successively declined over the past several years, which explains the contraction in revenue from EP's printing business. In our view, the outlook for the printing business remains dismal.

In 2020, EP diversified into the paper packaging business to seek a growth driver for its printing business in the wake of growing e-commerce and food-delivery demand. EP offers a wide range of paper packaging products, including paper bags, pizza boxes, tuck side boxes, paper crates, etc. In the first nine months of 2022, revenue from the packaging business reached THB208 million, a 15% increase y-o-y. Paper packaging is propelled by the prospect of heightening demand for food and beverage packaging, aided by the country's reopening. However, we project the printing and packaging businesses will represent a small slice of EP's earnings over the long term.

Tight liquidity

As of September 2022, the company had cash and cash equivalent of approximately THB750 million. FFO over the next 12 months are forecast to be about THB490 million. Meanwhile, EP had short-term and long-term debts coming due in the next 12 months, totaling THB2 billion. Therefore, we expect a large part of the debts to be refinanced. EP could raise funds by seeking project loans for its wind power projects or by issuing new debentures. With the ongoing development of the projects, we view the refinancing risk as manageable.

Debt structure

At the end of September 2022, EP had consolidated debt of THB4.5 billion. Most of the debt was made up of unsecured debentures at the company level, with an outstanding amount of THB3.9 billion. The ratio of priority debt to total debt was about 16%. However, the ratio may increase to over 50% once the wind farms obtain project loans.

BASE-CASE ASSUMPTIONS

- Revenue from printing and packaging of about THB700-THB800 million per year during 2022-2025, with a gross profit margin of around 10%-13%.
- Solar rooftop projects to produce power yield with a capacity factor of about 10%-11%.
- Energy yield of Vietnam wind farms to reach P90 (the 90% probability level of energy production).
- Revenue from power business of around THB100 million in 2022, THB800 million in 2023, and THB1.2 billion per year in 2024-2025.
- EBITDA margin of 22% in 2022, increasing to above 50% from 2023 onwards.
- Total capital expenditure of THB3.3 billion during 2022-2025.
- EP to obtain project finance loans of THB3.4 billion in 2023 for all its wind power projects in Vietnam.

RATING OUTLOOK

The "negative" outlook reflects the persistent uncertainties related to EP's wind power projects. We view EP's financial risk will become elevated if the projects face further serious delays in the commencement of commercial operations, or if cash generation is significantly lower than expected.

RATING SENSITIVITIES

We could consider revising the outlook to stable if EP's wind power projects start commercial operation, with performances in line with our expectations. Given the negative outlook, an upward rating revision is unlikely in the near term.

A rating downgrade could emerge as a result of continued weak cash generation. This could occur if EP's wind power projects encounter further serious delays in the commencement of operations, or they deliver weaker-than-expected cash flow due to significant tariff cuts or underperformance. A downgrade of the rating could also develop from new investments, which heighten the company's liquidity or financial risk.

COMPANY OVERVIEW

Formerly named Eastern Printing PLC (EPCO), EP was established in 1990 as a printing service provider. The company was listed on the Stock Exchange of Thailand (SET) in 1993. As of April 2022, Aqua Corporation PLC (AQUA) held approximately 47% of EP while the Chinsupakul family, the company's founder, owned 27%. EP provides a full range of printing services for both domestic and foreign customers. EP prints newspapers, magazines, product manuals, educational books, calendars, and advertising materials. The company has transitioned to focus heavily on the power business to make up for the drop-off

in the printing business. In April 2020, the company changed its name from EPCO to EP. EP's shares were moved from media and publishing to the energy and utility sector on the SET.

EP's power business is carried out by its main subsidiary, Eternity Power PLC (ETP; rated "BBB-/Negative"). EP currently owns 81% of ETP. EP launched its two pilot solar farms, with a total capacity of 11 MW, in 2012. The company later expanded with solar power projects in Thailand, Japan, and Vietnam.

The company also invested in two cogeneration power companies, generating and selling electricity under the small power producer (SPP) scheme, through 25-year power purchase agreements (PPAs) with the Electricity Generating Authority of Thailand (EGAT) and long-term contracts with industrial users.

In 2018, EP spent a total of THB490 million to acquire a 100% share of WPS (Thailand) Ltd. (WPS), which helped expand the company's printing facilities. For the power business, EP invested in two solar farms in Vietnam, namely "Xuan Tho 1" and "Xuan Tho 2".

In late 2019, EP sold off the two solar farms in Vietnam after they commenced operation. In 2020, EP sold all operating solar farms from its portfolio. Instead, EP invested in four wind farms in Vietnam, namely "Huong Linh 3" (HL3), "Huong Linh 4" (HL4), "Che Bien Tay Nguyen" (TN), and "Phat Trien Mien Nui" (MN). The four wind farms were initially slated to commence operation by the end of October 2021. EP sold its investments in the cogeneration power plants and small solar farms in Japan in 2021. Currently, EP's power portfolio has a total capacity of 168.7 MW.

KEY OPERATING PERFORMANCE

Table 1: Total Operating Revenue Breakdown

	2017	2018	2019	2020	2021	Jan-Sep 2021	Jan-Sep 2022
Printing business	47%	42%	37%	34%	54%	55%	50%
Packaging business	1%	1%	1%	7%	34%	35%	34%
Power business	52%	57%	62%	59%	12%	10%	16%
Total	100%	100%	100%	100%	100%	100%	100%
Total revenue (million THB)	931	979	1,530	1,145	700	517	608

Source: EP

Table 2: Power Project Portfolio (End of Sep 2022)

Project	Plant Type	Held by EP (%)	Installed (MW)	Equity (MWe)	SCOD/COD
Operating			7.9	6.4	
Solar rooftop	Solar rooftop	81.4	1.5	1.2	2014-2015
Commercial rooftop	Solar rooftop	81.4	6.4	5.2	2019-2020
Constructing & developing			160.8	128.7	
HL3	Wind farm	81.4	28.8	23.4	1H-2023
HL4	Wind farm	81.4	32.0	26.0	1H-2023
TN	Wind farm	77.3	50.0	38.6	1H-2023
MN	Wind farm	81.4	50.0	40.7	1H-2023
Total portfolio			168.7	132.5	

SCOD = Scheduled commercial operation date

COD = Commercial operation date

Source: EP

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS*

Unit: Mil. THB

	Jan-Sep 2022	-----Year Ended 31 December -----			
		2021	2020	2019	2018
Total operating revenues	615	722	1,168	1,552	1,052
Earnings before interest and taxes (EBIT)	29	139	320	786	550
Earnings before interest, taxes, depreciation, and amortization (EBITDA)	88	(3)	333	659	473
Funds from operations (FFO)	(161)	(953)	(35)	217	251
Adjusted interest expense	195	355	282	362	251
Capital expenditures	1,133	4,873	483	821	824
Total assets	10,104	11,530	8,382	11,555	10,599
Adjusted debt	4,043	2,520	2,162	6,433	6,336
Adjusted equity	4,829	5,270	4,862	3,897	3,280
Adjusted Ratios					
EBITDA margin (%)	14.38	(0.36)	28.54	42.45	44.95
Pretax return on permanent capital (%)	0.35 **	1.50	3.33	7.35	5.94
EBITDA interest coverage (times)	0.45	(0.01)	1.18	1.82	1.89
Debt to EBITDA (times)	46.63 **	(982.03)	6.48	9.77	13.41
FFO to debt (%)	(20.34) **	(37.84)	(1.63)	3.38	3.96
Debt to capitalization (%)	45.57	32.35	30.78	62.28	65.89

* Consolidated financial statements

** Annualized 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

Eastern Power Group PLC (EP)
Company Rating:

BBB-

Rating Outlook:

Negative

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