EASTERN POWER GROUP PLC

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CORPORATES

Company Rating:	BBB-
Outlook:	Stable

Last Review Date: 27/12/19

Company Rating History:

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

Contacts:

Narongchai Ponsirichusopol
narongchai@trisrating.com

Rapeepol Mahapant
rapeepol@trisrating.com

Parat Mahuttano
parat@trisrating.com

Monthian Chantarklam
monthian@trisrating.com

RATIONALE

TRIS Rating affirms the company rating on Eastern Power Group PLC (EP), formerly known as Eastern Printing PLC (EPCO), at "BBB-" with a "stable" outlook. The rating reflects EP's strong market presence in the printing industry and its predictable cash flow from the power business. However, the rating is tempered by the gloomy outlook of the printing industry and the risks associated with the wind power projects under development in Vietnam. The rating also recognizes challenging liquidity management during the construction period of the wind power projects.

KEY RATING CONSIDERATIONS

Strong presence in the printing business

EP has a strong market presence in the printing business, supported by its revenue size and broad range of products. EP's products comprise a variety of printing materials, including textbooks, manual, calendars, diaries, magazines, advertising materials, as well as local and international newspapers. In the fragmented market, EP's printing business is involved with a small number of large commercial printing companies.

The company maintains long-term relationships with its customers on the strength of its established track record. Despite disruption in the printing and publishing industries, EP's printing business remains profitable. Generally, the gross margin of the printing business is about 20%.

Printing industry still on a downward spiral

The printing business had been EP's core revenue contributor in the past. However, the industry has been disrupted by the rise of digital media. The demand for printing is tumbling, triggered by the fall of print media. The value of advertisements in print media has relentlessly declined over the past several years, which explains the contraction in EP's revenue from its printing business. In our view, the outlook for the printing business remains highly uncertain. The volume of printing appears to be a continued down spiral, given the fragile recovery of the overall economy.

Paper packaging to propel growth

EP sees paper packaging as the key growth driver for its printing business in the wake of growing e-commerce and food-delivery demand amid the Coronavirus Disease 2019 (COVID-19) pandemic. The company has invested in new packaging machinery. However, the production has just recently started in the back-half of 2020, a significant delay from our earlier expectation. Despite growth potential, EP faces with the challenge of building up a customer base amidst a fragmented market dominated by a small number of large paper packaging producers.

Softer-than-expected revenue from printing business

For the first nine months of 2020, EP's revenue in the printing business, including paper packaging, fell significantly short of our expectations. Total printing revenue came in at THB349 million, in contrast to around THB800 million in our previous full-year forecast. The revenue from newspaper, magazines, and catalog dropped as a result of lower demand induced by the COVID-19 outbreak. Meanwhile, the production and sales of paper packaging delayed from our expectation. In all, gross margin increased to 16% in the first nine months of 2020 from 13% in 2019. However, the gross profit margin was still lower than the range of 23%-25% EP achieved in 2016-2018. In our base-case forecast, we project EP's printing business to bring in THB670-THB760 million in total revenue during 2021-2023, which include revenue from paper packaging products of THB260-THB330 million. Overall gross profit margin is forecast at 18%.

Power business is the key revenue contributor

Currently, EP's revenue is largely driven by its power business. The company diversified into the solar power business in 2012 through its main subsidiary, Eternity Power PLC (ETP; rated "BBB-/Stable"). EP currently owns 75% of ETP. In the first nine months of 2020, power business contributed about 59% of total revenues. We expect the revenue contribution from the power business to drop temporarily to 26%, resulted from EP's recent divestiture of several operating power plants, before bouncing back to 62% when all developing wind farms in Vietnam are operational.

Change in the mix of power portfolio

Due to the dearth of opportunities and declining returns on investment in the domestic market, EP has been adjusting the mix of its power portfolio, to pursue growth and strengthen its capital structure. During 2019-2020, EP divested all of its operating solar farms with total capacity, in proportion to its ownership, of 127 megawatts (MW). In total, EP recognized gain on disposal of about THB2 billion. EP will use part of the proceeds to invest in four new onshore wind farms in Vietnam, with a combined capacity of 155 MW. The development and construction of the wind farms are in progress. When all of these new power projects are fully operational, we expect the new portfolio mix to significantly enhance EP's operating cash flow and improve the company's capital structure.

Predictable cash flow from power portfolio

The rating primarily reflects the predictable cash flow that EP gains from its power business. After the portfolio adjustment, EP holds a total capacity of 325 MW. Currently, the company owns four wind farms in Vietnam (155 MW), two solar farms in Japan (4 MW), a cluster of small-sized solar rooftops (8 MW), and investment in two cogeneration power plants (159 MW). Of the total capacity, power plants which are in operation have a combined capacity of 168 MW.

EP's solar rooftop projects in Thailand have secured long-term power purchase agreements (PPAs) with Metropolitan Electricity Authority (MEA) and private power buyers. The wind farms hold 20-year PPAs with Vietnam Electricity (EVN). The company receives fixed feed-in-tariff (FiT) under PPAs with MEA and EVN. All PPAs are on a non-firm basis.

EP has also invested in two cogeneration power plants, which have a combined contract capacity of 270 MW, under PPAs with the Electricity Generating Authority of Thailand (EGAT). In all, we view the cogeneration plants have a fair performance record as one of the two plants experienced an unplanned outage.

Challenging construction and operational risks

With the current portfolio mix, wind power will make up around 48% of total capacity while solar power will account for a minimal slice. In general, wind power requires high investment and more experience in project management. A wind farm development entails higher construction risks, relive to solar farms. The construction could be stretched out for a long period, given the high requirement of plant design and construction. Delay of construction and cost overrun could cause serious problem to project viability. In addition, wind power assets entail higher operational risks, such as mechanical and electrical breakdowns. The success of a wind power project largely hinges on the availability and the speed of wind. Small variations in average wind speed over time can make a significant deviation in power output.

Risk of lower tariff

The Vietnamese government set the 20-year FiT of US$8.5 cents per kilowatt-hour (kWh) for onshore wind power projects commissioned before 1 November 2021. The projects that fail to commence operation by the deadline are at risk of tariff cuts. Although partly mitigated by the terms of contract with the engineering, procurement, and construction (EPC) contractor, the construction risks of EP's wind power projects remain as a serious concern, given the tight timeline to meet the FiT longstop date. However, EP has a track record of successful development of large-scaled solar farms in Vietnam within a tight timeline.

Growing exposure in Vietnam

EP's growth strategy will broaden the company's exposure to Vietnam country risk. Vietnam's monsoonal climate and long coastlines explain the country's strategy for the wind power development. The demand for energy grows almost twice as fast as the gross domestic product (GDP). That said, power projects in Vietnam carry several risks, including changes in regulations, contract enforcement, and curtailment risks. We are also of the opinion that the credit profile of the state-run EVN is not as strong as the Thai state-owned power buyers.

Enhanced cash flow protection

As EP's operating projects were almost entirely divested, we expect the company's earnings will drop drastically in 2021, before staging a strong rebound in 2022. If the much-anticipated revenue from wind farms materializes as planned, we expect EP's operating cash flow and capital structure to improve significantly. In our base-case forecast, we project EP to start operating all wind farms by October 2021 and receive a FiT of US$8.5 cents per kWh. We project EP's revenue to slide to around THB900 million in 2021, but to surge to THB2 billion in 2022. At the same time, earnings before interest, taxes, depreciation, and amortization (EBITDA) are projected to tumble to THB200 million in 2021, before rising to around THB1 billion in 2022.

From 2022 onwards, funds from operations (FFO) are expected to be THB600 million a year, with the FFO to debt ratio to stay above 10%. With the previous mix of portfolio, we had projected the FFO to debt ratio to stay low at around 7% in our previous forecast. Therefore, this mirrors the expectation of heightened cash flow against debt obligation after the adjustment of portfolio.

Improved capital structure

Following the divestment, EP's adjusted debt sharply declined to THB1.3 billion as of September 2020, from THB6.4 billion as of 2019. In addition, the large gain on sales of power assets helped solidify EP's equity. In effect, the debt to capitalization ratio dropped to 22.3%, from 62.3% over the same period. We expect the company's leverage will remain low throughout 2021.

In our base-case, we expect EP to obtain financing from the EPC contractor to fund a significant portion of construction costs of the wind power projects. The EPC financing is planned to be replaced by project loans a year after the projects commence operation. The financing scheme helps lessen debt loads during the construction period.

As a result, adjusted debt is forecast to stay about THB1.8-THB1.9 billion in 2020-2021 before surging to THB6.4 billion in 2022. The debt to capitalization ratio is projected to peak at around 52% in 2022, before gradually declining. In our previous forecast based upon EP's preceding mix of portfolio, we had projected EP's debt to capitalization ratio to peak at about 65%.

Tight liquidity

We assess the company to have tight liquidity over the next 12 months. We see significant refinancing risk in relation to the company's debt profile, in particular the debentures coming due in 2021. The company also has to manage the funding requirement of the wind farm projects under construction. Meanwhile, EP is expected to experience the drastic falls in EBITDA and FFO in 2021, as a result of the divestment in solar assets.

As of September 2020, EP had cash on hand of approximately THB1.9 billion plus incoming cash receive of THB0.3 billion from the divestment. The available cash of approximately THB2.2 billion can accommodate the investment requirement in the wind farm projects since EP is required to pay around THB2.1 billion for the share purchase and equity injection to the projects. The rest of project developments are funded by the EPC financing. For the next 12 months, EP has debentures coming due of THB1.7 billion. The company would need to refinance the maturing debentures. We opine that the refinancing risk will be lessened with the progress of the wind power projects.

BASE-CASE ASSUMPTIONS

- Revenue from printing and packaging is estimated at THB670-THB760 million per year during 2021-2023, with a gross profit margin of around 18%.
- Solar rooftop projects to produce power at the 50% probability of level of energy production (P50). The wind farms to yield at P90.
- Revenue from power business to arrive at THB240 million in 2021 and surge to THB1.2 billion a year in 2022-2023.
- Total operating revenues to be THB900 million in 2021 and then increase to THB2 billion per annum during 2022-2023.
- EBITDA margin to decline to 22% in 2021 and then increase to stay at 55% from 2022 onwards.
- Total capital expenditure to be THB6.8 billion during 2020-2023.
- EP to obtain long credit terms from EPC contractor for the construction of the wind power projects in Vietnam.
- Dividend pay-out to be THB100 million per year.

RATING OUTLOOK

The "stable" outlook reflects our expectation that EP's new wind farm projects will progress as planned and the projects will perform in line with expectations. We also expect the packaging production line will perform satisfactorily and steer the printing business out of its revenue slump. Moreover, we expect EP to prudently manage liquidity over the course of its new wind farm development.

RATING SENSITIVITIES

A rating upgrade is unlikely in the next 12-18 months. On the contrary, downward rating pressure would emerge if the wind farm projects face significant delay and/or cost overrun, which considerably hurt the returns of the projects, or if the performances of the projects fall significantly short of expectations. Moreover, downward revision to the rating could develop if EP engages in additional sizable investment, which leads to heightened 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 September 2020, Aqua Corporation PLC (AQUA) held approximately 38% of EP while the Chinsupakul family, the company's founders, owned 17%. EP provides a full range of printing services, serving 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 moved from media and publishing sector to energy and utilities sector in the SET.

EP diversified into the solar power business in 2012, primarily through its main subsidiary, "Eternity Power PLC" (ETP). EP currently owns 75% of ETP. EP launched its two pilot solar farm projects in Kanchanaburi province, with a total capacity of 11 MW in 2012. In 2013, EP added a solar farm project in Lopburi province, with a capacity of 6 MW. During 2014-2015, the company invested in eight solar rooftop projects in Bangkok and Samutprakan province, with aggregate contracted capacity of 1.5 MW.

EP later expanded solar power projects in Thailand and Japan, as well as cogeneration power. EP has invested in PPTC Co., Ltd. (PPTC) and SSUT Co., Ltd. (SSUT). Both companies produce cogeneration power under the small power producer scheme (SPP), through 25-year PPAs with EGAT and long-term contracts with industrial users. EP also added a solar farm in Prachinburi province to its portfolio with capacity of 5 MW. In addition, EP added up 44 MW into the portfolio by expanding to invest in five solar farms in Japan.

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 effect, EP owned four solar farms in Thailand, five solar farms in Japan, two solar farms in Vietnam, and a cluster of solar rooftop power plants in Thailand. Total capacity measured in proportion to EP's ownership was at 137 MW. Apart from the renewable power plants, EP also held an investment in two cogeneration power plants which added up total capacity to 296 MW.

In late 2019, EP sold off the two solar farms in Vietnam after they commenced operation. In 2020, ETP 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 are slated to commence operation by end of October 2021. As a result, EP holds a total capacity of 325 MW.

KEY OPERATING PERFORMANCE

Table 1: Revenue Breakdown

	2015	2016	2017	2018	2019	Jan-Sep 2019	Jan-Sep 2020
Printing business	57%	58%	47%	41%	37%	37%	33%
Power business	40%	39%	50%	53%	61%	61%	59%
Others	3%	3%	3%	6%	2%	2%	8%
Total	100%	100%	100%	100%	100%	100%	100%
Total revenue (million THB)	**890**	**881**	**963**	**1,052**	**1,556**	**1,140**	**1,054**

Source: EP

Table 2: Power Project Portfolio (After the Divestment)

Project	Plant Type	Held by EP (%)	Installed (MW)	Equity (MWe)	SCOD/COD
OPERATING			**366.9**	**166.0**	
Solar rooftop	Solar rooftop	100	1.5	1.5	Sep-14
Commercial rooftop	Solar rooftop	100	5.4	5.4	2018-2019
PPTC	CCGT [(1)]	51	120.0	60.8	Mar-16
SSUT	CCGT [(1)]	41	240.0	98.3	Dec-16
CONSTRUCTING & DEVELOPING			**164.2**	**159.2**	
SHICHI KACHUKU1, 2	Solar farm	98	4.4	4.3	2021
HL3	Wind farm	100	28.8	28.8	Oct-21
HL4	Wind farm	100	32.0	32.0	Oct-21
TN	Wind farm	90	49.5	44.6	Oct-21
MN	Wind farm	100	49.5	49.5	Oct-21
Total portfolio			**531.1**	**325.2**	

Remark: [(1)] Combined cycle gas turbine
Source: ETP

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS*

Unit: Mil. THB

	Jan-Sep 2020	---------------Year Ended 31 December ---------- 2019	2018	2017	2016
Total operating revenues	1,054	1,556	1,052	955	880
Earnings before interest and taxes (EBIT)	369	790	550	466	264
Earnings before interest, taxes, depreciation, and amortization (EBITDA)	491	663	473	434	371
Funds from operations (FFO)	212	231	201	200	240
Adjusted interest expense	205	362	251	211	115
Capital expenditures	116	821	824	935	1,092
Total assets	9,074	11,555	10,599	8,508	6,930
Adjusted debt	1,332	6,433	6,336	5,472	2,608
Adjusted equity	4,640	3,897	3,280	2,473	2,191
Adjusted Ratios					
EBITDA Margin (%)	46.58	42.59	44.95	45.46	42.15
Pretax return on permanent capital (%)	5.22 **	7.39	5.94	6.22	5.73
EBITDA interest coverage (times)	2.40	1.83	1.89	2.05	3.24
Debt to EBITDA (times)	2.21 **	9.71	13.41	12.60	7.03
FFO to debt (%)	14.72 **	3.60	3.17	3.66	9.19
Debt to capitalization (%)	22.31	62.27	65.89	68.87	54.35

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

RELATED CRITERIA

- Rating Methodology – Corporate, 26 July 2019
- Key Financial Ratios and Adjustments, 5 September 2018
- Group Rating Methodology, 10 July 2015

Eastern Power Group PLC (EP)

Company Rating:	BBB-
Rating Outlook:	Stable

TRIS Rating Co., Ltd.
Silom Complex Building, 24th Floor, 191 Silom Road, Bangkok 10500, Thailand Tel: 0-2098-3000