

EASTERN POWER GROUP PLC

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CORPORATES

Company Rating: BBB-
Outlook: Stable

Last Review Date: 30/12/20

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-” with a “stable” outlook. The rating reflects the expected reliability of earnings to be derived from EP’s wind power projects in Vietnam, EP’s strong market position in the printing industry, and growth prospect of its paper packaging business. The rating also takes into consideration EP’s heightened liquidity after its divestment of cogeneration power plants. Conversely, the rating is weighed down by the dim outlook of printing industry, the lingering execution risks of the wind power projects in Vietnam, and a more challenging environment of renewable power business.

KEY RATING CONSIDERATIONS

Expected reliable earnings from wind farms

EP is formerly known as Eastern Printing PLC, with its core business in printing services. The company subsequently diversified into power business, and succeeded in developing a number of solar power projects in Thailand, Japan, and Vietnam. On the whole, EP’s power portfolio has consistently delivered satisfactory performance.

Following its divestiture of several operating power plants, EP’s revenue from the power business is derived from a small cluster of solar rooftop projects which render revenue of only THB80-THB90 million per year. EP is currently developing four wind farms in Vietnam, with net capacity of around 126 megawatts (MW). EP’s future earnings therefore heavily rely on the success of the project.

Given its past records of successful project executions, we expect EP will complete the development of the wind power projects. The rating embeds our expectation that the wind farms will steadily bring in sizable earnings in the years ahead. The reliability of cash flow will be backed by multi-year power purchase agreements (PPAs) signed with the state-run Vietnam Electricity (EVN), fixed tariff, and expected satisfactory performances of the wind farms.

Wind farms will enlarge earnings

In our base-case forecast, we project EP to start operating its first three wind farms in March 2022, with a combined capacity of 100 MW. The remaining projects carrying 26 MW capacity will commence operation in June 2022. All projects will receive a feed-in-tariff (FiT) of US\$8.5 cents per kilowatt-hour (kWh). When fully operational, we expect the wind farms will generate THB1 billion in earnings before interest, taxes, depreciation, and amortization (EBITDA) a year.

Pandemic-induced delay in constructions

Several wind power developers in Vietnam have been affected by the fallout of the Coronavirus Disease 2019 (COVID-19) pandemic, with delays in the manufacturing and transportation of wind turbines. Project construction and the installation of equipment have also been severely affected by travel restrictions and lockdowns. Similar delays occurred to EP’s wind power projects in Vietnam. As of mid-December 2021, the construction progress of EP’s two wind farms in Quang Tri province (76.6 MW) was about 80%-90% while the other two wind farms in Gia Lai province (49.5 MW) had slower

progress. As a result, the expected revenue from EP's power business in 2021 and 2022 appears to be significantly weaker than our previous projection.

Risk of tariff cut

The Vietnamese government set the 20-year FiT of US\$8.5 cents per 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. As EP's wind power projects already miss the FiT longstop date, they may no longer be eligible for the favorable FiT. Wind power developers have requested the Vietnamese government for extension of deadline. Although the Vietnamese government's decision on the request is still pending, we assume EP will continue to receive the offered tariff in our forecast. That said, further delays in project completion will jeopardize the expected cash flow.

In addition to construction risks, 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 the speed of wind. Small variations of wind speeds over time may result in a significant deviation in power outputs. The performances of EP's very first wind farms will need to be proven.

Solid market position in the printing business

In the printing business, EP has solid market position as a leading printing service provider, backed by its size and broad range of products. The company maintains long-term relationships with its customers on the strength of its long-established track record. Despite disruption in the printing and publishing industries, EP's printing business remains profitable. Gross margin of the printing business is generally about 15%-20%.

However, the printing industry has been on a persistent decline, fueled by the rapid growth of internet usage and digital media. EP's revenue from printing business has consistently tapered to THB393 million in 2020, declining from the range of THB410-THB560 million in the prior years. The prolonged COVID-19 pandemic has added further pressure on printing demand. For the first nine months of 2021, EP's revenue from the printing business stood at THB285 million, marking a 5% drop in revenue year-over-year (y-o-y). Moreover, the printing profit margin was significantly compressed by higher paper cost caused by the pandemic induced supply bottlenecks.

Potential growth in paper packaging

In response to the downfall of printing demand, EP is leaning towards paper packaging which has strong growth potential. EP offers a wide range of paper packaging products, including paper bags, pizza boxes, tuck side boxes, paper crates, etc. For the first nine months of 2021, packaging revenue was THB180 million, representing a 254% increase from the same period in the previous year. EP plans to expand its customer base to retail customers via online-platforms and discount stores. Therefore, sales of paper packaging are expected to grow, together with improving profit margins. On the whole, gross profit from printing and packaging businesses was 14% in the first nine months of 2021.

Divestment of cogeneration power plants

In December 2021, EP sold its subsidiary, Eastern Cogeneration Co., Ltd. (E-COGEN), to Univentures BGP Co., Ltd. (UVBGP), the joint ventures between Univentures PLC (UV) and B. Grimm Power PLC (BGRIM). E-COGEN holds shares in PPTC Co., Ltd. (PPTC) and SSUT Co., Ltd. (SSUT), which own three cogeneration power plants under the small power producer scheme (SPP). The cogeneration power plants hold 25-year PPAs with the Electricity Generating Authority of Thailand (EGAT) and long-term contracts with industrial users. After the divestment, EP's power portfolio capacity reduced by around half to 132.5 MW as measured in proportion to EP's ownership. However, we view the divestment does not impact EP's EBITDA as the cogeneration power plants are not distributing dividends, due to their long-pending disputes with the engineering, procurement, and construction (EPC) contractor.

Enhanced liquidity

The divestment transaction will significantly enhance EP's liquidity. We expect EP to receive cash of THB10.9 billion, net of arbitration reserve, and to recognize profit of THB2.2 billion from the divestment. In our forecast, EP will spend about THB6.3 billion to repay short-term debts and hold remaining cash balance of THB4.5 billion at the end of 2021. EP plans to pay the remaining project cost of the wind farms under construction by cash since the projects no longer obtain financing from the EPC contractor. We expect EP will pay the remaining cost of wind farms totaling THB2.1 billion in 2022, the amount of which could be fully covered by the available cash from divestment. Therefore, construction risks of the wind farms are partly mitigated.

Improvement in cash flow against debt

In total, we project EP's revenue to slide to around THB615 million in 2021, and to increase to THB1.7 billion in 2022 and reach THB2.1 billion a year in 2023-2024. At the same time, EBITDA are projected to increase to THB0.8 billion in 2022 and THB1.1 billion a year in 2023-2024.

In our base-case forecast, we expect the debt to EBITDA ratio of EP will improve to range 3-5 times by 2023, as opposed to 6-13 times in the recent past. We project its funds from operations (FFO) will arrive at THB500 million in 2022 and around THB700 million a year in 2023-2024. The FFO to debt ratio will increase to 10% in 2022 and reach 20% in 2023. We also forecast the debt to capitalization ratio to improve to 25.4% in 2021 from 30.8% in 2020. Looking ahead, we expect EP will keep the debt to capitalization ratio at around 40%, well below the levels of 60%-70% over the past years.

More challenging business environment

We hold our view that the domestic power market has become more challenging. Competition has intensified in recent years in the wake of the government's decentralization policy to control electricity costs to consumers. Private companies, ranging from very small entrepreneurs to large conglomerates, have branched into power business. While the demand for power tends to grow modestly due to the pandemic-led slowdown, the country is currently saddled with high excess reserve of capacity. Thai power companies are leaning towards investments outside Thailand, due to the cut-off of incentive tariff, intense bidding competition, repeated delays in public projects, and contracted return on investment. However, some overseas expansions entail higher country risk stemming from transparency and consistency of regulations, credit profiles of off-takers, and environmental challenges.

Substantial exposure in Vietnam

EP has substantial exposure in Vietnam. Its power plants in Vietnam will represent almost 100% of its total power production capacity when all wind farms commence their operations in 2022. For a full-year operation, the wind farms will account for about 90% of the company's total EBITDA. In addition, EP still looks for more opportunity in Vietnam with a greater amount of investment. Despite fast-growing demand for electricity, we view that investments in Vietnam carry several risks, including changes in regulations, contract enforcement, insufficient infrastructure, and construction delays. In addition, the counterparty risk is noticeably higher. We view the credit profile of EVN is not as strong as the Thai state-owned power buyers. In addition, high debt-funded investment will weigh negatively on the rating.

Capital structure

At the end of September 2021, EP had debt of THB9.7 billion. Most of debt was at the subsidiary level, which is considered as priority debt. This means the ratio of priority debt to total debt was about 69%. As its priority debt ratio is more than the threshold of 50%, we view that EP's unsecured creditors are significantly disadvantaged with respect to the priority of claim against EP's assets. After the divestment of cogeneration power, we project the priority debt ratio will temporarily fall below 50%, or about 34%. However, we expect the ratio will bounce back to over 50% once the wind farms obtain project financing.

BASE-CASE ASSUMPTIONS

- Revenue from printing and packaging is estimated at THB580-THB840 million per year during 2021-2024, with a gross profit margin of around 14%-16%.
- Solar rooftop projects to produce power yield with the capacity factor of 13%.
- Energy yield of Vietnam wind farms to be at P90 (the 90% probability level of energy production).
- Revenue from power business to arrive at THB0.9 billion in 2022 and surge to THB1.3 billion a year in 2023.
- EBITDA margin to stay at 45% in 2022 and increase to above 50% from 2023 onwards.
- Total capital expenditure to be THB8 billion during 2021-2024.
- EP to obtain project finance loan of THB5.5 billion in 2022 for all wind power projects in Vietnam.
- Dividend payout to be THB46-THB300 million per year during 2021-2024.

RATING OUTLOOK

The "stable" outlook reflects our expectation that EP's wind farm projects will commence operation as forecast and the projects will perform in line with expectations. We also expect the company's packaging business 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 may occur if EP could generate higher-than-expected cash flow from operation on a sustained basis, which leads to a considerable improvement in the level of cash flow against debt obligations. Conversely, downward rating pressure would emerge if EP's cash flow from operations come in far below our forecast. This could arise from further delays in commencement of wind farms operation, a tariff cut, or significant underperformance. Moreover, downward revision to the rating could also 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 November 2021, Aqua Corporation PLC (AQUA) held approximately 39.6% of EP while the Chinsupakul family, the company's founder, owned 22.7%. 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 utility sector in the SET.

EP diversified into the solar power business in 2012, primarily through its main subsidiary, Eternity Power PLC (ETP; rated "BBB-/Stable"). EP currently owns 81.4% in 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. In total, EP's capacity measured in proportion to its ownership was at 296 MW.

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 slated to commence operation by end of October 2021. As a result, EP held a total capacity of 292 MW.

In 2021, EP sold its investment in three cogeneration power plants and small solar farms in Japan. As a result, EP's power portfolio capacity reduces to 132.5 MW.

KEY OPERATING PERFORMANCE

Table 1: Total Operating Revenues Breakdown

	2016	2017	2018	2019	2020	Jan-Sep 2020	Jan-Sep 2021
Printing business	60%	47%	42%	37%	34%	31%	55%
Packaging business	0%	1%	1%	1%	7%	5%	35%
Power business	40%	52%	57%	62%	59%	64%	10%
Total	100%	100%	100%	100%	100%	100%	100%
Total revenue (million THB)	855	931	979	1,530	1,145	972	517

Source: EP

Table 2: Power Project Portfolio (End of Dec 2021)

Project	Plant Type	Held by EP (%)	Installed (MW)	Equity (MWe)	SCOD/COD
Operating			6.9	6.4	
Solar rooftop	Solar rooftop	81.4	1.5	1.2	2014-2015
Commercial rooftop	Solar rooftop	81.4	5.4	5.2	2019-2020
Constructing & developing			159.8	126.1	
HL3	Wind farm	81.4	28.8	23.4	1H-2022
HL4	Wind farm	81.4	32.0	26.1	1H-2022
TN	Wind farm	73.3	49.5	36.3	1H-2022
MN	Wind farm	81.4	49.5	40.3	1H-2022
Total portfolio			166.7	132.5	

Source: EP

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS

Unit: Mil. THB

	Jan-Sep 2021	-----Year Ended 31 December -----			
		2020	2019	2018	2017
Total operating revenues	526	1,187	1,552	1,052	955
Earnings before interest and taxes (EBIT)	525	334	786	550	466
Earnings before interest, taxes, depreciation, and amortization (EBITDA)	397	347	659	473	434
Funds from operations (FFO)	105	10	227	201	200
Adjusted interest expense	229	282	362	251	211
Capital expenditures	3,032	483	821	824	935
Total assets	14,206	8,382	11,555	10,599	8,508
Adjusted debt	9,596	2,162	6,433	6,336	5,472
Adjusted equity	4,078	4,862	3,897	3,280	2,473
Adjusted Ratios					
EBITDA margin (%)	75.39	29.24	42.45	44.95	45.46
Pretax return on permanent capital (%)	4.46	3.47	7.35	5.94	6.22
EBITDA interest coverage (times)	1.73	1.23	1.82	1.89	2.05
Debt to EBITDA (times)	37.99	6.23	9.77	13.41	12.60
FFO to debt (%)	(1.02)	0.47	3.54	3.17	3.66
Debt to capitalization (%)	70.18	30.78	62.28	65.89	68.87

RELATED CRITERIA

- Group Rating Methodology, 13 January 2021
- Rating Methodology – Corporate, 26 July 2019
- Key Financial Ratios and Adjustments, 5 September 2018

Eastern Power Group PLC (EP)

Company Rating:	BBB-
Rating Outlook:	Stable

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