

EASTERN SUGAR AND CANE PLC

No. 160/2021
30 September 2021

CORPORATES

Company Rating: BBB
Outlook: Stable

Last Review Date: 24/09/20

Company Rating History:

Date	Rating	Outlook/Alert
04/06/20	BBB	Negative
30/01/20	BBB	Stable

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RATIONALE

TRIS Rating affirms the company rating on Eastern Sugar and Cane PLC (ESC) at “BBB”. At the same time, the rating outlook is revised to “stable” from “negative”.

The outlook revision reflects the easing of concerns over ESC’s weakening financial profile from the prolonged and severe drought in Thailand and the plunge in the worldwide sugar price.

The rating continues to reflect ESC’s long track record in the sugar industry, diverse sources of income, and acceptable financial leverage. These strengths are partially offset by ESC’s small size and the inherent volatility faced by producers of commodity products like sugar.

KEY RATING CONSIDERATIONS

Expected recovery from drought and plummeting sugar prices

We expect ESC’s performance to revive during the forecast years. Sugarcane production volume should increase during the 2022-2023 season due to improved rainfall for cane plantations. In addition, the sugar price has picked up from its lowest level in ten years in April 2020 and should remain at its five-year average rate (14-15 cents per pound) or above during 2021-2023.

Thailand’s total sugarcane output for the 2020/2021 production period was 67 million tonnes, lower than the 75 million tonnes recorded in the 2019/2020 season, leading to an expected fall in revenue to THB6.1 billion in 2021. Nonetheless, ESC’s earnings before interest, taxes, depreciation, and amortization (EBITDA) margin is likely to be 20% in 2021, the same as in 2020.

As a result of good rainfall in 2021, Thailand’s sugarcane volume for the 2021/2022 season should reach 80 million tonnes. The world sugar price is assumed to remain around 14-16 cents per pound in 2022 and 2023. Therefore, ESC’s revenue is forecast to increase to THB7 billion in 2022 and THB7.9 billion in 2023. EBITDA is projected at THB1.2-THB1.5 billion per annum in 2021-2023.

According to the company’s management, ESC reported revenue and EBITDA of THB4.2 billion and THB536 million, respectively, in the first half of 2021, achieving approximately 70% and 45% of our 2021 forecast. This forecast has already taken into account the impact of low sugarcane production in the 2020/2021 season.

Improved profitability despite softening revenue

ESC has achieved relatively stable profitability despite the cyclical nature of sugar prices and sugarcane supplies, partly thanks to the steady cash flow generated by the company’s energy business (ethanol and electricity). The EBITDA margin hovered in the 14%-20% range during 2015-2020. Although revenue in 2020 was lower than in 2019, the EBITDA margin in 2020 was higher at 20%, compared with 14% in 2019.

The company’s EBITDA margin is expected to remain in the 19%-20% range during the forecast years since we expect a turnaround in sugarcane volume and sugar price.

Lengthy experience in the sugar industry

ESC has been in Thailand's sugar industry for more than 60 years. The company is one of just eight producers in Thailand to have received the "Bonsucro" standard certificate. Raw sugar is ESC's main sugar product, contributing approximately 52% of total sugar sales in 2020. Export sales contributes 73% of total sugar sales in 2020. Most of ESC's export customers are international traders.

ESC has focused on value-added products such as very high polarization (VHP) sugar, white sugar, and refined sugar over the past five years. The contribution from raw sugar has gradually decreased and the product mix changed from 64% in raw sugar and 36% in value-added products in 2016 to 52% in raw sugar and 48% in value-added products in 2020. Premium sugar yields a higher profit margin and attracts more customers.

ESC is also focusing more on sales to domestic channels. The contribution from domestic sales has increased to around 30% in 2020 from 10% of total sugar sales in 2018. Domestic prices are higher than export prices and the domestic logistic costs are lower, leading to better margins.

Diversified income stream

ESC has expanded along the sugar value chain in order to maximize the utilization of sugarcane and by-products of the sugar manufacturing process. ESC's major sugar-related businesses are electricity generation and ethanol production.

ESC's power plants have a combined installed power generation capacity of 123.6 megawatts (MW). Bagasse, a by-product of sugar production, and sugarcane leaves are used as biofuel for electricity generation. The company sells electricity to two state-owned enterprises under long-term power purchase agreements (PPA). The Electricity Generating Authority of Thailand (EGAT) purchases 40 MW of electricity under the Small Power Producer (SPP) scheme while the Provincial Electricity Authority (PEA) buys 11 MW under the Very Small Power Producer (VSPP) scheme.

ESC has an ethanol production capacity of 150,000 liters per day. Buyers of ethanol are the major oil companies in Thailand.

Revenue from the energy business (electricity and ethanol) has increased steadily and now makes up a significant portion of the company's total revenue. In 2020, revenue from the energy segment accounted for 22% of ESC's total revenue; the sugar business made up 70%, and the balance came from fertilizer and other services to farmers.

Acceptable leverage and cash flow protection

Under our base-case scenario, we expect ESC's leverage to remain at the same level as 2020 for the next three years. Most upcoming capital expenditures will be used to develop process improvements such as energy efficiency, implementation of a new software system, and purchase of sugarcane harvesters. We expect the company's debt to capitalization ratio to be 51% in 2021, and the net debt to EBITDA to be 5 times in 2021 before gradually improving to 4.4 times in 2022 and 4 times in 2023.

We assess ESC to have adequate liquidity over the next 12 months. The ratio of funds from operations (FFO) to total debt will likely increase to 20% in 2023 from 16% in 2021. We expect the EBITDA interest coverage ratio to be in the range of 8-9 times during 2021-2023. We also expect ESC to have sufficient credit facilities from commercial banks and internal cash flow to fund future capital expenditures.

BASE-CASE ASSUMPTIONS

- Revenues to be THB6.1 billion in 2021, then improving by 15% to THB7 billion in 2022 and by another 13% to THB7.9 billion in 2023 due to improved rainfall and a rebound in the sugar price.
- EBITDA margin of around 20% during 2021-2023.
- Capital expenditures (CAPEX) of THB550-THB750 million during the forecast period.

RATING OUTLOOK

The "stable" outlook reflects our expectation that ESC will be able to revive its operating performance while maintaining an acceptable capital structure, following an easing of concerns over the prolonged and severe drought in Thailand and the plunge in the worldwide sugar price.

RATING SENSITIVITIES

A rating upside case could occur if ESC enlarges its earnings and stabilizes its profit margin without weakening its balance sheet. On the other hand, a rating downside case could emerge if profitability and earnings fall significantly short of expectations. Any overly aggressive, debt-funded investments that would materially weaken the company's balance sheet

and cash flow protection could also lead to a downgrade scenario.

COMPANY OVERVIEW

ESC was established in 1959 by the Wattanavekin family. As of December 2020, the Wattanavekin family collectively held 98.6% of the company's shares.

ESC's sugar plants are located in the eastern region of Thailand. Sugarcane, the main raw material to produce sugar, is a cool-weather crop grown primarily in eastern and northeastern Thailand.

In the eastern region, ESC is the only sugar producer in Sa Kaeo province; other sugar mills are located in Chonburi province. The sugarcane plantation area in Sa Kaeo province represents 68% of the total sugarcane plantation area in the eastern region. Consequently, ESC does not have to compete with other producers to secure sufficient supplies of sugarcane to feed its mills. ESC also enjoys strong relationships with sugarcane growers. The company offers broad-based support to growers, including advances of cash and fertilizer, development of planting techniques, advanced irrigation techniques, and breeding and harvesting tools.

ESC's first mill at Wattana Nakorn district has production capacity of 40,000 tonnes cane per day (TCD). ESC received approval in July 2018 to build a second mill at Wang Sombun district, Sa Kaeo province. The new mill has a capacity of 18,000 TCD. The first phase of 8,000 TCD started up in December 2018. As of June 2021, ESC had total production capacity of 48,000 TCD.

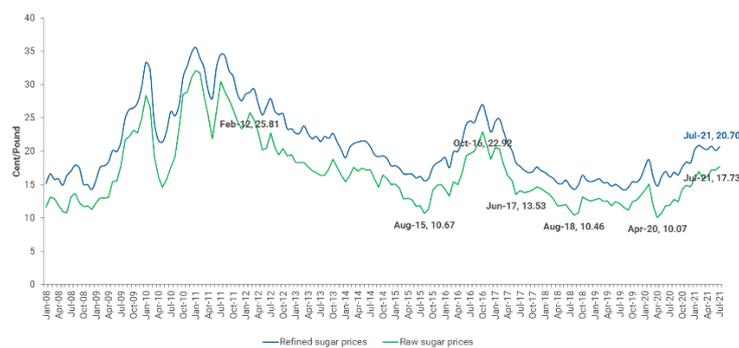
In the 2020/2021 production period, ESC procured 2.8 million tonnes of sugarcane and produced 316,464 tonnes of sugar. ESC's market share, in terms of tonnes of sugar produced in Thailand, was 4.2%. For comparison, the two market leaders held market shares of around 22.1% and 16.4%, respectively.

ESC's sugar package size is 50 kilograms (kg) while the sale size is 100 kg. Currently, ESC sells white and refined sugar in the domestic market. It exports raw sugar, VHP sugar, and refined sugar.

ESC's sugar-related businesses include the production of electricity, ethanol, and fertilizer, as well as research and development and logistics services.

KEY OPERATING PERFORMANCE

Chart 1: Raw Sugar Price Worldwide



Note: Monthly prices of Futures Contract No.11

Source: New York Board of Trade, United States Department of Agriculture (USDA)

Table 1: Sugar Production in Thailand

Unit: Mil tonnes

Sugar Producers	2016/ 2017	2017/ 2018	2018/ 2019	2019/ 2020	2020/ 2021
Mitr Phol	1.98	2.73	2.92	1.61	1.68
Thai Roong Ruang	1.42	2.13	2.42	1.34	1.24
KSL Group	0.72	1.20	1.14	0.58	0.53
Thai Ekkalak	0.94	1.19	1.03	0.60	0.47
ESC	0.38	0.51	0.49	0.34	0.32
Banpong	0.44	0.52	0.58	0.38	0.27
Wangkanai	0.39	0.79	0.69	0.22	0.24
Khonburi	0.27	0.44	0.37	0.19	0.23
Kumpawapee	0.28	0.41	0.39	0.24	0.17
Others	3.21	4.79	4.55	2.79	2.44
Total	10.03	14.71	14.58	8.29	7.59

Source: Office of the Cane and Sugar Board (OSCB)

Table 2: ESC's Revenue Breakdown by Business

Unit: %

Product	2016	2017	2018	2019	2020
Sugar sales	74	74	66	68	70
Ethanol sales	12	11	15	14	13
Electricity sales	6	7	9	9	9
Fertilizer sales	5	5	6	5	4
Service and others	3	3	4	4	4
Total sales	100	100	100	100	100
Total sales (mil. THB)	7,815	8,472	7,897	7,154	6,592

Source: ESC

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS*

Unit: Mil. THB

	-----Year Ended 31 December -----				
	2020	2019	2018	2017	2016
Total operating revenues	6,994	7,315	8,200	8,557	7,911
Earnings before interest and taxes (EBIT)	431	130	683	919	745
Earnings before interest, taxes, depreciation, and amortization (EBITDA)	1,387	1,053	1,421	1,604	1,368
Funds from operations (FFO)	1,271	780	1,144	1,294	1,128
Adjusted interest expense	134	248	228	225	203
Capital expenditures	494	677	1,755	973	1,588
Total assets	13,745	12,833	13,628	12,038	10,525
Adjusted debt	5,891	6,108	6,234	4,417	4,926
Adjusted equity	5,589	5,364	5,515	5,072	4,460
Adjusted Ratios					
EBITDA margin (%)	19.83	14.39	17.34	18.75	17.29
Pretax return on permanent capital (%)	3.56	1.11	6.33	9.51	7.77
EBITDA interest coverage (times)	10.36	4.24	6.23	7.13	6.72
Debt to EBITDA (times)	4.25	5.80	4.39	2.75	3.60
FFO to debt (%)	21.57	12.77	18.34	29.30	22.90
Debt to capitalization (%)	51.31	53.24	53.06	46.55	52.48

* Consolidated financial statements

RELATED CRITERIA

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

Eastern Sugar and Cane PLC (ESC)

Company Rating:	BBB
Rating Outlook:	Stable

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