TRIS RATING
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SRI TRANG AGRO-INDUSTRY PLC

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CORPORATES

Company Rating:	BBB+
Issue Ratings:	
Senior unsecured	BBB+
Outlook:	Stable

Company Rating History:

Date	Rating	Outlook/Alert
27/10/17	BBB+	Stable
05/08/11	A-	Stable
20/11/10	BBB+	Positive
30/09/09	BBB+	Stable
14/09/07	BBB	Stable

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RATIONALE

TRIS Rating affirms the company rating on Sri Trang Agro-Industry PLC (STA) and the ratings on its senior unsecured debentures at "BBB+", with a "stable" outlook. The ratings reflect the company's leading position in the natural rubber (NR) industry, the benefits of vertical integration, and the extensive track record of the management team. However, these strengths are partially offset by the cyclical and volatile nature of prices for natural rubber as well as the economic slowdowns in rubber importing countries.

KEY RATING CONSIDERATIONS

Strong business profile

STA has a competitive advantage arises from its strong market position as the world's leading NR processer and merchandiser, its extensive network of raw material sources, and an experienced management team. STA's market share, in terms of sales volume of NR products worldwide, varied from 9%-12% in 2013-2017. STA's market share in the first half of 2018 was 10%.

The company sells rubber products to well-known tire manufacturers, such as Bridgestone and Goodyear. Exports account for 80%-85% of STA's NR sales volume annually. The largest NR's export market for the past five years has been China. Exports to China comprised 52%-58% of STA's NR international sales volume. Other countries in Asia, such as Singapore, Korea, Japan, and India represented totaling around 28%-37% of export sales volume.

New profit-focused strategy

STA's profit margin is very thin and fluctuates along with rubber prices and exchange rates. The company can partially mitigate the negative impacts of the aforementioned risk by utilizing to hedging transactions. The operating income before depreciation and amortization as a percentage of sales (including a provision or reversal on the diminution in value of inventories and gains or losses from derivatives instruments) ranged from 0.22%-3.57% during 2013-2017. Earnings before interest, tax, depreciation, and amortization (EBITDA) ranged between Bt579-Bt3,109 million during the same period.

Since the beginning of 2018, STA has implemented a new profit-focused strategy that emphasizes high-margin products such as gloves and concentrated latex. As a result, the operating profit margin rose to 6.75% during the first half of 2018. The higher operating margin pushed EBITDA to Bt2,534 million during the first half of 2018, up from Bt1,228 million over the same period of 2017.

TRIS Rating believes that STA's operating profit margin before depreciation and amortization will improve and stay at 5%-6% during 2018-2021. Moreover, production growth from recovery in the auto industry and global economic situation support a positive outlook.

Acceptable capital structure

Total debt declined to Bt25,272 million as of June 2018, down from Bt32,306 million as of December 2017. STA's need for working capital fell and the company did not make any major investments during the first half of 2018. The total debt to capitalization ratio was 50.35% at the end of June 2018, compared with 47%-61% during 2015-2017.

In our forecast, capital expenditures will vary widely from 2018 through 2021. Capital expenditures will range from Bt800 million to Bt2,700 million per year during 2018-2021. Most of the spending is earmarked for capacity expansions, specifically at the block rubber processing plants and glove production plants.

A drop in leverage and gains from derivative instruments is forecast to push cash flow protection up during 2018-2021. The EBITDA interest coverage ratio is forecast to improve to 4.0-5.0 times, compared with 0.8-2.8 times in 2015-2017. The funds from operations (FFO) to total debt ratio is forecast at 10.5%-12.5% over 2018-2021, up from 0.4%-8.1% during 2015-2017.

Ample liquidity

Over the next 12 months, liquidity is assessed to be adequate. Almost 60% of STA's outstanding debts, or Bt14,349 million, are short-term debts. The short-term borrowings are utilized to finance inventory and accounts receivable. Inventory of NR are typically highly liquid and marketable. It can be easily liquidated to pay down debts.

Scheduled long-term debt and debentures repayments will amount to Bt1,200-Bt3,000 million per year in 2019-2021. Cash and cash equivalents were Bt3,223 million at the end of June 2018. Unused credit facilities of more than Bt20,000 million from a number of banks will help the company manage these repayments. Our base case forecast assumes EBITDA will increase to Bt4,000-Bt4,500 million per year in 2018-2021 following STA's selective selling strategy and better inventory management.

RATING OUTLOOK

The "stable" outlook reflects the expectation that STA will maintain its competitive position in the NR industry as it shifts to focus on high-margin products. Liquidity is forecast to remain ample, and the balance sheet is expected to stay strong enough to withstand the effects of volatile rubber prices.

RATING SENSITIVITIES

STA's credit upside could result from the successful implementation of new profit-focused strategy that boost its credit metric on a sustained basis. The downside case could occur if rubber prices stay low, leading to noticeably weakening debt serviceability for a sustained period. Any aggressive debt-funded investment would also be a negative factor for STA's credit ratings.

COMPANY OVERVIEW

STA is the world's leading processor and merchandiser of NR. The company has 40 processing plants for block rubber, ribbed smoked sheet, concentrated latex, and gloves. The plants are located in Thailand, Indonesia, and Myanmar. As of 30 June 2018, total optimum processing capacity of NR was 2,180,160 tonnes per year and glove production capacity was 15.7 billion pieces per year.

Approximately 83% of its NR products are sold directly to customers, which are mostly tyre manufacturers. Exports accounted for 83% of total sales volume. China was the largest export market, accounting for 48% of export volume during the first half of 2018.

Sales volume in the rubber gloves segment is split between two types: latex gloves and nitrile examination gloves. Latex gloves made up 60% of sales volume in this segment during the first half of 2018; nitrile examination gloves made up the balance. The vast majority, around 80%-85% of gloves, is sold as private label brands. STA sells the balance under its own brand names, such as "Sri Trang Gloves", "I'm glove" and other brands.

STA exports gloves to over 100 countries around the world. The main markets are the United States (US) and the European countries, which typically accounted for 50% of gloves sales volume. STA is putting more effort into penetrating emerging markets such as India, China, Africa and Latin America. Emerging markets offer higher growth potential. Customers in the emerging markets show a preference for latex gloves, which carry a higher profit margin than nitrile gloves.

Currently, the major NR producing nations are Thailand, Indonesia, Vietnam, and Malaysia. In the first three months of 2018, these four countries accounted for 80% of the NR produced worldwide. Thailand was the largest producer, with a total production volume of 1.30 million tonnes, followed by Indonesia (0.88 million tonnes), Vietnam (0.22 million tonnes), and Malaysia (0.18 million tonnes). In terms of consumption, demand for NR worldwide has increased from 11.43 million tonnes in 2010 to 13.23 million tonnes in 2017. It grew at an average of 3.7% per annum. China consumes around 40.1%. Worldwide NR consumption slightly rose by 6.53% in the first half of 2018 following a faster pace of growth in the total output of tyres from emerging and mature markets.

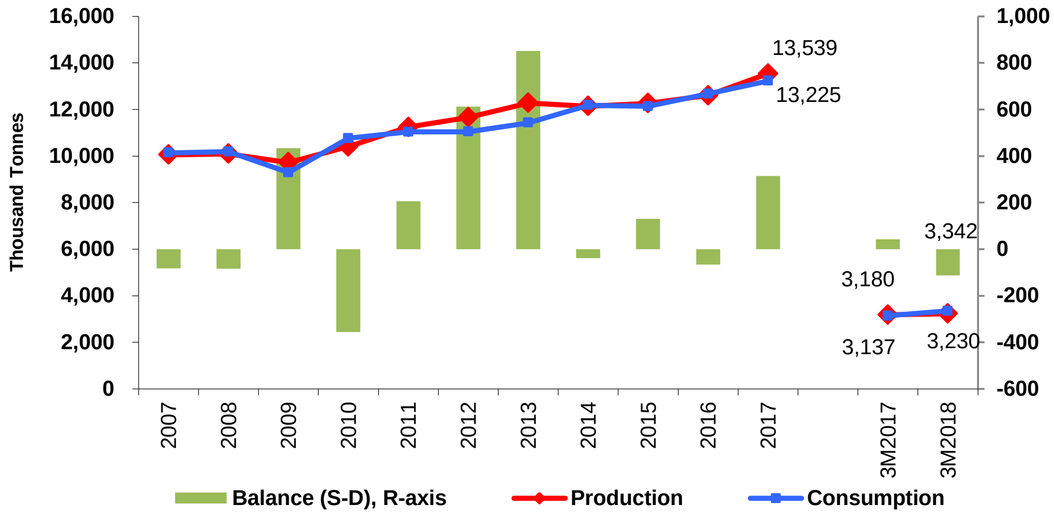
Recent development

STA and Semperit Technische Produkte Gesellschaft m.b.H. (STPG), an Austrian former joint venture (JV) partner in Sri Trang Gloves (Thailand) Co., Ltd. (STGT) had reached agreements to settle all legal proceeding and demergered the JV in March 2017. STA acquired an additional 50% stake in STGT, with total net investment cost of Bt4,400 million. STA's business profile will strengthen somewhat in the long term as it will have more contribution from STGT's glove operations, which are in the downstream sector of the NR industry.

STA is in the process of amalgamating the operations of STGT and the operations of Thaikong Co.,Ltd (TK) into a new entity. TK produces powdered latex gloves. The amalgamation is expected to complete by April 2019. Once complete, STA's group will hold directly and indirectly 81.08% of the shares of the newly formed entity. The amalgamation will yield several benefits. For example, production capacity for gloves will increase by 4,000 billion pieces per year, from 17.2 billion pieces per year by the end of 2018, to 21.2 billion pieces per year by April of 2019. The amalgamation will also boost efficiency and increase the utilization of resources, increasing the value of the rubber gloves segment.

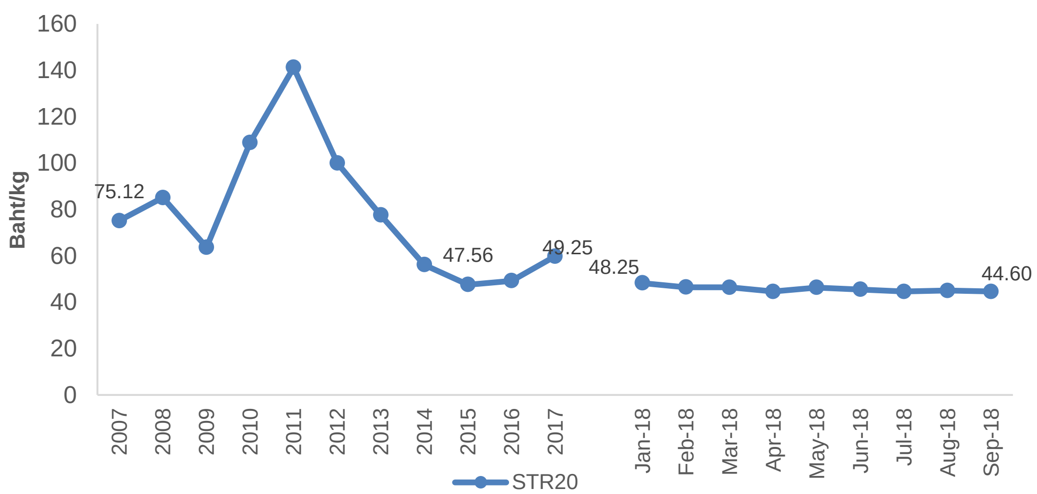
KEY OPERTING PERFORMANCE

Chart 1: World Production and Consumption of Natural Rubber



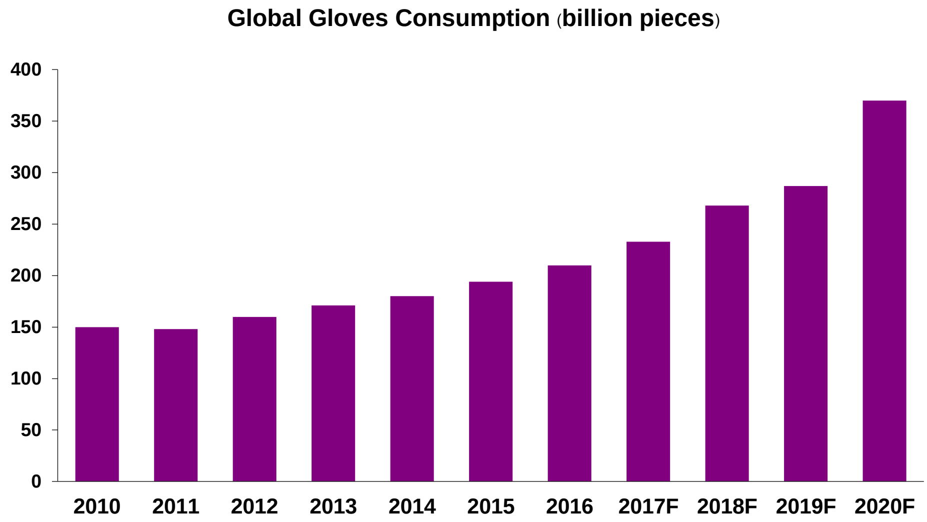
Source: International Rubber Study Group (IRSG)

Chart 2: Thailand's Natural Rubber Prices



Source: Rubber Authority of Thailand (RAOT)

Chart 3: Global Gloves Consumption



Source: Malaysia Rubber Glove manufacturers Association (MARGMA)

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS

Unit: Bt million

	Jan-Jun 2018	---------------- Year Ended 31 December ------------ 2017	2016	2015	2014
Total operating revenues	37,583	89,565	77,410	61,439	75,657
Adjusted interest expense	2,537	198	536	2,194	1,775
Operating income	1,487	(1,036)	(306)	2,004	1,766
Earnings before interest and taxes (EBIT)	2,534	3,109	579	2,493	2,722
Earnings before interest, taxes, depreciation, and amortization (EBITDA)	1,726	1,818	130	1,584	2,000
Funds from operations (FFO)	652	1,271	732	878	681
Capital expenditures	1,559	3,167	2,295	2,617	3,011
Total assets	54,866	59,708	55,959	43,879	37,791
Adjusted debt	22,587	30,600	30,469	17,326	12,114
Adjusted equity	24,919	23,277	19,912	21,334	20,592
Adjusted Ratios					
Operating income as % of total operating revenues (%)	6.75	0.22	0.69	3.57	2.35
Pretax return on permanent capital (%)	4.20	(1.92)	(0.66)	5.29	4.73
EBITDA interest coverage (times)	3.89	2.45	0.79	2.84	3.99
Debt to EBITDA (times)	5.12	9.84	52.66	6.95	4.45
FFO to debt (%)	12.17	5.94	0.43	9.14	16.51
Debt to capitalization (%)	47.55	56.80	60.48	44.82	37.04

Sri Trang Agro-Industry PLC (STA)

Company Rating:	BBB+
Issue Ratings:	
STA195A: Bt810 million senior unsecured debentures due 2019	BBB+
STA215A: Bt1,455 million senior unsecured debentures due 2021	BBB+
Rating Outlook:	Stable

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