CHAROEN POKPHAND FOODS PLC

No. 67/2018
8 May 2019

CORPORATES

Company Rating:	A+
Issue Ratings:	
Senior unsecured	A+
Hybrid	A-
Outlook:	Stable

Last Review Date: 08/11/18

Company Rating History:

Date	Rating	Outlook/Alert
31/03/15	A+	Stable
20/06/14	AA-	Negative
19/05/11	AA-	Stable
30/04/10	A+	Positive
22/06/06	A+	Stable
20/05/05	A	Positive
12/07/04	A	Stable
28/05/04	A	
01/03/01	A+	

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RATIONALE

TRIS Rating affirms the company rating on Charoen Pokphand Foods PLC (CPF) and the ratings on CPF's senior unsecured debentures at "A+". We also affirm the rating on CPF's unsecured subordinated perpetual debentures (hybrid debentures) at "A-".

The ratings continue to reflect the company's leading position in the Thai agribusiness and food industry, as well as the geographic diversity of its operations, and diverse range of product offerings and markets served. The ratings also reflect the efforts to create more branded food products, as well as the financial flexibility the company gains from its strategic investments. However, these strengths are partially offset by high leverage, the inherent cyclicality of commodity-type products and the cost of grain, the exposure to disease outbreaks, and changes in regulations imposed by importing countries.

KEY RATING CONSIDERATIONS

Swine prices recover in Vietnam

CPF's operating results improved in 2018, largely driven by a rise in swine prices in Vietnam. After a slump in 2017, the price of swine in Vietnam recovered in the second quarter of 2018. The rise was due to a resolve of oversupply situation in Vietnam.

The ease of oversupply pushed up prices and boosted CPF's operating results. The average price of swine in Vietnam surged by 51% year-on-year (y-o-y) to 43,309 Vietnam dong (VND) per kilogram (kg.), according to information provided by CPF. As a result, the operating profit margin of the livestock operation abroad improved to 6.8% in 2018 from 1.4% in 2017.

Nonetheless, the domestic livestock segment reported a loss. A supply glut led to a slump in the price of chicken (broilers). The operating profit margin of the domestic livestock segment was -2.1% in 2018, compared with 1.9% in 2017. The operating profit margin of the aquaculture segment also weakened, slipping to 7.5% in 2018 from 9.2% in 2017.

Overall, the rise in the livestock segment abroad offset the weaker performance in the domestic segment. The operating margin before depreciation and amortization improved to 7.8% in 2018 from 6.2% in 2017. Earnings before interest, tax, depreciation, and amortization (EBITDA) was Bt47.3 billion in 2018, up from Bt35.6 billion in 2017.

Operating profit will continue rising in 2019. Several factors are responsible for the rise: rising swine prices, increased export of chicken, and stable feed costs. However, CPF will continue to face several challenges, such as the appreciation of Thai baht and the risk of a widespread swine epidemic. Under TRIS Rating's base case scenario, CPF's operating revenue will range around Bt576-Bt654 billion over 2019-2021. EBITDA is expected to hover around Bt51-Bt60 billion per annum.

Leverage will stay high

Ongoing and sizable capital expenditures and acquisitions pushed up the leverage to increase. The adjusted debt rose to Bt331.9 billion in 2018 from Bt299.6 billion in 2017. The debt to capitalization ratio rose to 61.1% in 2018 from 57.8% in 2017.

TRIS Rating forecasts CPF's leverage will stay high over the next few years. To pursue its growth strategy, CPF has laid out plans for sizeable capital expenditures, accounting to Bt20-Bt30 billion per year, excluding acquisitions. CPF will continue to explore new investment opportunities as long as an acquisition or investment is aligned with its core business and generates a reasonable profit. Under TRIS Rating's base case scenario, the debt to capitalization ratio of CPF will hover around 60% over the next few years despite the aggressive growth strategy.

Cash flow protection improves

Cash flow protection has improved as profits increased. The EBITDA interest coverage ratio was 3.4 times in 2018, compared with 2.6 times in 2017. The ratio of funds from operations (FFO) to total debt was 8.2% in 2018, up from 7.1% in 2017. As of December 2018, adjusted debt amounted Bt331.9 billion. Debentures and long-term loans made up about 70% of total debt. The remainder was short-term loans to finance CPF's working capital needs. The current ratio was fine around 1.0 times with no mismatch fund.

CPF's liquidity and financial flexibility remain strong. Scheduled debt repayments of approximately Bt27,000 million are due in 2019. Primary source of repayment shall be from the cash flow from operation. Liquidity buffer is acceptable with total cash on hand and short-term securities of around Bt33 billion at the end of 2018. Additionally, CPF has number of large investment in marketable securities. These investments give CPF additional financial flexibility. For example, CPF holds a 34.2% stake in CP All PLC (CPALL), the leading convenience store operator in Thailand. The market capitalization of CPALL was approximately Bt211 billion as of 31 December 2018.

Leading position in the Thai agribusiness and food industry

CPF's strong business profile reflects its leading position in Thailand's agribusiness and food industry. In several lines of business in Thailand, CPF is the largest producer. In the feed segment, it holds about half of the total market for shrimp feed, based on production volume, and about one-third of the market for livestock feed. In the Thai poultry and swine segment, CPF accounts for 25% of the domestic production of poultry and 18% of the domestic production of swine. As one of the nation's largest integrated producers, CPF benefits significantly from economies of scale.

Geographic diversification and diverse range of products

CPF's operational risk is partly mitigated by the geographic diversity of its operations and markets. As of 31 March 2019, CPF had production bases in 17 countries on five continents. The operations in Thailand accounted for 33% of total revenue in 2018, while the operations abroad contributed 67%. China operations contributed 26% of total revenue, followed by operations in Vietnam (15%). The other major sources of revenue were Taiwan, the United States (US), India, Russia, Turkey, and Cambodia. Sales in each of these nations accounted for 1%-4% of total revenue in 2018.

CPF's revenue sources are geographically diverse. Sales in Thailand comprised only 28% of total sales in 2018. The Asian region, a growing market, has become the largest source of sales, accounting for 58% of total sales in 2018. The European Union (EU) nations and the US accounted for only 10% and 4% of total sales in 2018, respectively. CPF's continued effort to broaden its geographic coverage will gradually alleviate the impact from disease outbreaks and trade barriers.

A diverse range of products partly reduces the volatility of earnings. CPF is a fully integrated producer of livestock and shrimp products. The company's product portfolio includes animal feed, poultry, shrimp, swine, and food products. In 2018, feed was the largest revenue contributor, providing 42% of total sales, followed by poultry, swine and shrimp farming (41%), and food products (17%).

BASE CASE ASSUMPTIONS

- Revenues of CPF will grow by 6%-7% per annum over the next three years.
- The gross profit margin is forecast at 13%-14%, the adjusted operating margin will stay around 8%.
- The EBITDA interest coverage ratio is expected to hold at about 3 times, while the FFO to total debt ratio is projected to stay at 8%-9%.
- Excluding acquisitions, capital spending will be Bt30 billion per year over the next three years.

RATING OUTLOOK

The "stable" outlook reflects TRIS Rating's expectation that CPF will maintain its leading position in the dynamic agribusiness and food industry. The company's diverse range of operations, products, and markets is expected to provide some insulation from the cyclical nature of commodity-like farm products and from disease epidemics.

RATING SENSITIVITIES

Any rating upside hinges on CPF's ability to strengthen its capital structure significantly and demonstrate a material, sustainable improvement in debt serviceability. In contrast, the ratings would likely be downgraded should any debt-funded acquisitions materially deteriorate the balance sheet and weaken cash flow protection. Should operating performance fall much below the anticipated levels, a downgrade could follow.

COMPANY OVERVIEW

Founded in 1978, CPF is Thailand's largest agribusiness and food conglomerate. As of 7 March 2019, CPG Group [1] held 53.9% of CPF's shares. CPF's business is divided into two segments, livestock and aquaculture, with three types of operations in each segment: feed, farm, and food. Revenue from feed products contributed 42% of total sales in 2018. Farm products and food products generated 41% and 17% of total sales, respectively.

CPF is a fully-integrated producer of swine, chicken, and shrimp products. Its fully-integrated operations help its products meet international standards, making its products qualified for export to the major markets such as EU countries, Japan, and the US.

CPF expanded abroad in 2002. By March 2019, operations expanded to cover 17 countries. Operations abroad accounted for 67% of total sales in 2018, while domestic sales were 28% and export sales were 5%.

In order to insulate itself from the price fluctuations inherent in commodity-type products, CPF is pursuing a long-term strategy of focusing on value-added products. CPF has continued to broaden its portfolio of products and markets as well as adding new distribution channels through several acquisitions. The investments include an integrated pork producer in Canada, plus several food service suppliers in Europe, shrimp farm in Brazil, as well as restaurants in Thailand and Vietnam.

Recent Development: Recently, CPF through its subsidiary signed the share purchase agreement to acquire Canadian pork producer HyLife Group Holdings Ltd. (HyLife) for CA$498 million (Bt11.8 billion). The acquisition would make CPF a 50.1% owner of HyLife, with the remainder held by its Japanese partner, Itochu Corporation. The investment would give it access to a pork production base and opportunity to expand in North America and premium markets such as Japan. The transaction which is subject to approval from Canada's agricultural approvals and anti-trust filing is expected to close during the last quarter of 2019.

KEY OPERATING PERFORMANCE

Table 1: CPF's Revenue Breakdown

Unit: %

By Product	2014	2015	2016	2017	2018
Feed	53	52	48	45	42
Farm	35	36	40	37	41
Food	12	12	12	18	17
Total	100	100	100	100	100
Sales (Bt mil.)	**426,039**	**421,355**	**464,465**	**501,507**	**541,937**

Source: CPF

Table 2: CPF's Revenue Breakdown by Geography

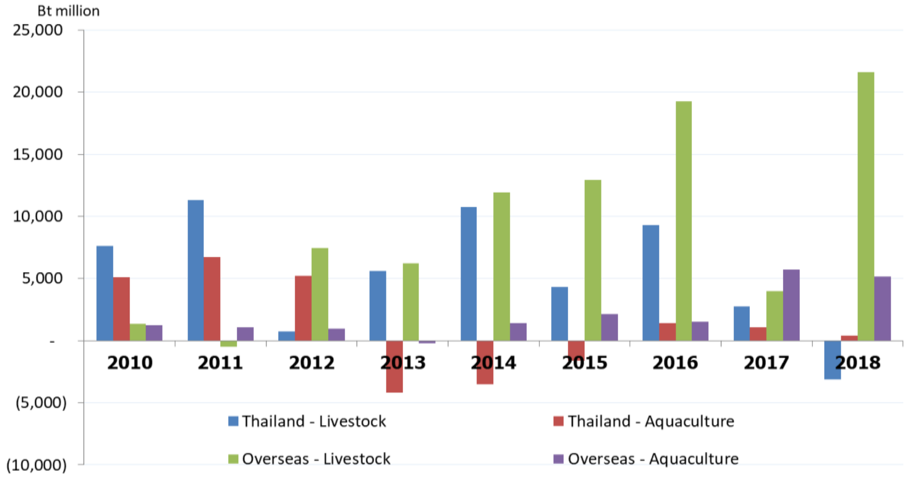
Unit: %

Country	2014	2015	2016	2017	2018
Thailand	34.8	33.4	32.3	29.5	27.5
EU	8.4	7.9	9.4	10.2	10.0
Asia	55.2	57.3	57.2	54.7	57.8
USA	1.4	1.0	0.8	5.2	4.4
Others	0.2	0.4	0.3	0.4	0.2
Total	**100**	**100**	**100**	**100**	**100**

Source: CPF

[1] *CPG Group is a reporting group to be in compliance with Section 246 and Section 247 of the Securities and Exchange Act of 2535.*

Chart 1: CPF's Operating Profit by Business Unit



Source: CPF

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS

Unit: Bt million

	----------------------Year Ended 31 December ---------------------				
	2018	2017	2016	2015	2014
Total operating revenues	545,068	503,734	466,792	424,768	428,193
Operating income	42,684	31,056	46,218	30,356	30,243
Earnings before interest and taxes (EBIT)	31,733	21,258	38,039	23,699	23,380
Earnings before interest, taxes, depreciation, and amortization (EBITDA)	47,319	35,564	51,102	35,026	33,880
Funds from operations (FFO)	27,212	21,463	31,623	20,337	20,067
Adjusted interest expense	13,895	13,850	12,267	11,035	10,163
Capital expenditures	29,009	30,639	22,576	25,725	25,958
Total assets	628,091	593,497	582,179	494,262	416,764
Adjusted debt	331,898	299,600	299,378	239,252	178,064
Adjusted equity	211,158	219,142	193,706	173,725	163,966
Adjusted Ratios					
Operating income as % of total operating revenues (%)	7.83	6.17	9.90	7.15	7.06
Pretax return on permanent capital (%)	5.66	3.94	7.68	5.65	6.52
EBITDA interest coverage (times)	3.41	2.56	4.17	3.17	3.33
Debt to EBITDA (times)	7.01	8.42	5.86	6.83	5.26
FFO to debt (%)	8.20	7.14	10.56	8.50	11.27
Debt to capitalization (%)	61.12	57.76	60.72	57.93	52.06

RELATED CRITERIA

- Hybrid Securities Rating Criteria, 12 September 2018
- Key Financial Ratios and Adjustments, 5 September 2018
- Rating Methodology – Corporate, 31 October 2007

Charoen Pokphand Foods PLC (CPF)

Company Rating:	A+
Issue Ratings:	
CPF198A: Bt6,000 million senior unsecured debentures due 2019	A+
CPF198B: Bt2,500 million senior unsecured debentures due 2019	A+
CPF204A: Bt3,060 million senior unsecured debentures due 2020	A+
CPF20NA: Bt6,700 million senior unsecured debentures due 2020	A+
CPF205A: Bt6,500 million senior unsecured debentures due 2020	A+
CPF218A: Bt3,000 million senior unsecured debentures due 2021	A+
CPF218B: Bt5,500 million senior unsecured debentures due 2021	A+
CPF225A: Bt7,600 million senior unsecured debentures due 2022	A+
CPF228A: Bt4,000 million senior unsecured debentures due 2022	A+
CPF235A: Bt5,500 million senior unsecured debentures due 2023	A+
CPF237A: Bt1,940 million senior unsecured debentures due 2023	A+
CPF244A: Bt3,500 million senior unsecured debentures due 2024	A+
CPF24NA: Bt2,200 million senior unsecured debentures due 2024	A+
CPF251A: Bt5,460 million senior unsecured debentures due 2025	A+
CPF257A: Bt3,000 million senior unsecured debentures due 2025	A+
CPF277A: Bt2,000 million senior unsecured debentures due 2027	A+
CPF281A: Bt6,540 million senior unsecured debentures due 2028	A+
CPF28NA: Bt3,200 million senior unsecured debentures due 2028	A+
CPF30NA: Bt5,300 million senior unsecured debentures due 2030	A+
CPF314A: Bt2,500 million senior unsecured debentures due 2031	A+
CPF328A: Bt5,000 million senior unsecured debentures due 2032	A+
CPF41DA: Bt6,000 million senior unsecured debentures due 2041	A+
CPF418A: Bt4,000 million senior unsecured debentures due 2041	A+
CPF17PA: Bt15,000 million subordinated capital debentures	A-
Rating Outlook:	Stable

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