

EASTERN WATER RESOURCES DEVELOPMENT AND MANAGEMENT PLC

No. 119/2023
30 June 2023

CORPORATES

| | |
|------------------------|--------|
| Company Rating: | A |
| Issue Ratings: | |
| Senior unsecured | A |
| Outlook: | Stable |

Last Review Date: 11/01/23

Company Rating History:

| Date | Rating | Outlook/Alert |
|----------|--------|------------------|
| 29/06/22 | A | Stable |
| 25/02/22 | A+ | Negative |
| 23/01/08 | A+ | Stable |
| 20/09/07 | A+ | Alert Developing |
| 12/07/04 | A+ | Stable |
| 29/06/04 | A+ | - |

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RATIONALE

TRIS Rating affirms the company rating on Eastern Water Resources Development and Management PLC (EASTW) and the ratings on its senior unsecured debentures at “A”, with a “stable” outlook. The ratings reflect EASTW’s strength as a major raw water supplier with a comprehensive pipeline network in the Eastern Economic Corridor (EEC), its reliable services and lengthy track record, and its strong profitability. These strengths are partially offset by its increasing leverage from some major investments in new water pipelines.

KEY RATING CONSIDERATIONS

Competition expected to intensify

We expect intense competition of raw water sales in the EEC, following the entry of a new raw water supplier to the market. EASTW lost its monopoly status after the Treasury Department selected a new private operator to lease and manage its pipeline network in the EEC in 2021. This network spans 136 kilometers (km) and includes the Dok Krai water pipeline, the Nong Pla Lai – Nong Khor water pipeline, and the Nong Khor – Laem Chabang (phase I & II) water pipeline. In April 2023, EASTW transferred the Nong Pla Lai–Nong Khor and Nong Khor–Laem Chabang (phase II) pipelines, totaling 59 km, to the new operator. The remaining leased water pipelines must be transferred to the new operator by the end of December 2023.

As of 31 May 2023, EASTW’s main and distribution pipelines had a total length of 464 km, consisting of its owned pipelines (387 km) and leased pipelines from the Treasury Department (77 km). Based on 2022 figures, raw water sold through the Treasury Department’s pipelines accounted for approximately 61% of EASTW’s total raw water distribution volume.

Continue as a major raw water supplier in EEC

We believe EASTW will continue to be a key supplier of raw water in the EEC. EASTW is developing 136 km of new water pipelines, including 94 km of pipelines alongside the Treasury Department’s pipelines and a new 42-km pipeline connected to the Klong Luang Reservoir. The new pipelines are expected to be completed by the end of 2023. Consequently, EASTW’s water pipeline system will be able to supply raw water to customers in parallel with those of the Treasury Department operated by the new operator.

Overall, the company’s water pipeline network will total around 523 km, connecting various government reservoirs, rivers, and privately owned reservoirs. This comprehensive pipeline network is a key competitive strength of the company, as it provides more reliable access to various water sources, especially during periods of drought. In 2022, the company sourced water from both government and privately owned reservoirs totaling approximately 427 million cubic meters (MCM) per year at current capacity. Water extraction accounted for 67% of EASTW’s total water resources in 2022.

Barriers to entry are high for newcomers, due to high investment costs and the difficulty in obtaining permits from relevant agencies to install pipelines and extract water.

Higher water demand to alleviate lease expiration impact

We expect the expiration of the leased pipelines to have a limited impact on EASTW due to the strong demand for both raw water and industrial water in the EEC area. According to our base-case forecast, the company's volume of raw water sales in 2023 will decline by 10% due to the transfer of two Treasury Department pipelines in April 2023. During 2024-2025, we anticipate EASTW to retain 70%-80% of the existing customers from the Treasury Department's pipelines after the new operator assumes control of all the Treasury Department pipelines. However, we expect the demand for raw water to remain strong due to the recovered industrial activities, coupled with the likelihood of drought during 2024-2025. Additionally, the company plans to sell more industrial water in tandem with the committed volumes to its clients. Therefore, we project that EASTW's total revenue will slightly decline to around THB4.0 billion in 2023 and then rebound to THB4.2-THB4.5 billion per year in 2024-2025.

Profitability to stay strong despite at a lower level

We expect EASTW's profitability to remain satisfactory, despite the increased competition after losing the Treasury Department pipelines contracts to the new operator. Price pressure is expected to be high. The average raw water price in 2024-2025 is expected to be 5% lower than the current level due to the competition. However, EASTW's earnings before interest, taxes, depreciation and amortization (EBITDA) are likely to remain at a healthy level of around THB1.8-THB2.0 billion per year throughout the forecast years. This could mean around 10%-15% lower than the levels of THB2.0-THB2.4 billion per year recorded during 2015-2022. EBITDA margin is likely to decline to around 45% in the years ahead, from the 48%-55% range during 2015-2022.

New pipeline investments to push up leverage

EASTW is developing new pipelines to replace pipelines of expired operating rights and to retain existing customers. The investment is expected to cost around THB5.6 billion.

We expect EASTW's leverage to increase gradually during the forecast period, to support planned capital expenditure (CAPEX) of around THB4.2 billion in 2023 and THB1.5 billion per year in 2024-2025. Apart from the add-on CAPEX to build new pipelines to replace pipelines of expired operating rights, EASTW plans to invest in new pipelines to cope with the rising demand from its customers and to mitigate impacts from droughts that are hard to predict. This includes a new pipeline connected to the Klong Luang Reservoir which is expected to increase water supplies in Chonburi province from 2023 onwards.

The remaining CAPEX will be used to upgrade the capabilities of the water grid in the EEC and to develop technology and facilities for total water solutions. We expect EASTW's adjusted debt to capitalization ratio to climb to around 55% in 2023-2025. The adjusted net debt to EBITDA ratio is likely to rise to 8 times in 2023-2025.

At the end of March 2023, EASTW's adjusted debt to capitalization ratio was 51%. The net debt to EBITDA ratio was 5.9 times for the first three months of 2023.

Acceptable liquidity

We assess EASTW to have adequate liquidity over the next 12 months. Its sources of funds comprised cash on hand and short-term investments of THB1.0 billion and undrawn credit facilities of THB2.7 billion at the end of March 2023. Its funds from operations (FFO) over the next 12 months are projected to be around THB1.4 billion. These sources of funds should be sufficient to cover debt services and investment needs over the next 12 months. EASTW has long-term debt repayment obligations of around THB1.6 billion coming due in the next 12 months, and an investment budget for 2023 of around THB4.2 billion. The company also plans to issue new THB2.9 billion debentures to finance its investments.

EASTW should have no problems complying with its debenture covenants over the next 12 to 18 months. The debt-to-equity ratio at the end of March 2023 was 1.2 times, well below the debentures covenant of 2 times. Priority debt accounted for 4% of total debt as of 31 March 2023.

BASE-CASE ASSUMPTIONS

- EASTW to retain 70%-80% of its customers from expired pipelines.
- Total revenues to be THB4.1-THB4.5 billion per year in 2023-2025.
- EBITDA margin at around 45% in 2023-2025.
- Total capital spending of THB4.2 billion in 2023, and THB1.5 billion per year in 2024-2025.

RATING OUTLOOK

The “stable” outlook reflects the expectation that EASTW will be able to retain the majority of its customers and continue its cash generation in line with our projection, despite competition from the newcomer.

RATING SENSITIVITIES

A rating upgrade is unlikely in the near term. However, a downgrade could occur if EASTW’s operating performance falls significantly short of our expectations. This could occur if the company loses significant numbers of customers or is unable to build new water pipelines to replace those previously leased from the Treasury Department.

COMPANY OVERVIEW

EASTW was established in 1992 by a Cabinet resolution. The government granted EASTW a mandate to develop and manage raw water distribution systems in the EEC. As of May 2023, EASTW’s major shareholders were the Provincial Waterworks Authority (PWA; owning a 40.2% stake); Manila Water Company, Inc. (MWC; 18.7%); and the Industrial Estate Authority of Thailand (IEAT; 4.6%).

In 2022, EASTW sold a total of 230 MCM of raw water. Currently, EASTW supplies raw water in Chonburi, Rayong, and Chachoengsao provinces. The company has a strategy to focus more on comprehensive water solutions, covering raw water, tap water, industrial water, wastewater management, and recycled water.

EASTW, through its subsidiary, Universal Utilities PLC (UU), provides tap water services in 12 areas with a total production capacity of 398,900 cubic meters (cu.m.) per day in 2022. Excluding construction revenue under concession agreements, raw water sales accounted for 61% of the company’s total revenue, while tap water services represented 33% of the total in 2022.

In 2018, EASTW signed 25-year and 30-year contracts with Gulf PD Co., Ltd. and Amata Water Co., Ltd. to supply industrial water of 22 MCM per year and 5.5 MCM per year, respectively. Revenues from these industrial water contracts have been recognized from 2021 onwards.

In 2020, the company entered into four agreements to provide total water solutions in the EEC area: a 25-year concession to provide tap water and wastewater treatment services to U-Tapao Airport; a 20-year contract for the supply of industrial water to Carabao Group PLC (CBG); a 30-year contract to supply tap water to PTT PLC at Wang Chan Valley; and a 32-year contract for the supply of raw water to Thai Oil PLC (TOP).

KEY OPERATING PERFORMANCE
Table 1: EASTW's Total Revenue Breakdown by Line of Business

| Line of Business | Unit | 2018 | 2019 | 2020 | 2021 | 2022 | Jan-Mar 2022 | Jan-Mar 2023 |
|---|----------|------------|------------|------------|------------|------------|--------------|--------------|
| Raw water | % | 57 | 61 | 59 | 64 | 61 | 65 | 62 |
| Tap water | % | 34 | 32 | 35 | 31 | 33 | 29 | 33 |
| Industrial water | % | - | - | - | - | 1 | 1 | 2 |
| Engineering services and rental | % | 4 | 3 | 3 | 3 | 3 | 3 | 3 |
| Construction revenue under concession agreement | % | 6 | 4 | 3 | 2 | 2 | 2 | 0 |
| Total | | 100 | 100 | 100 | 100 | 100 | 100 | 100 |
| Revenue from sale & service | Mil. THB | 4,221 | 4,680 | 4,204 | 4,631 | 4,263 | 1,137 | 1,113 |

Source: EASTW

Table 2: EASTW's Pipelines

| | Pipelines | Length (Km) | % of Total | Transfer Pipelines | Raw Water Distribution Volume in 2022 (MCM) | % to Raw Water Distribution Volume in 2022 |
|---|--|-------------|-------------|--------------------|---|--|
| | Pipelines leased from Treasury Department | | | | | |
| 1 | Dok Krai-Mapthaphut- Sattahip | 48.3 | 9% | 31 Dec 2023* | 81 | 31% |
| 2 | Nong Khor – Laem Chabang (phase I) | 29.1 | 6% | 31 Dec 2023* | 34 | 13% |
| 3 | Nong-Pla Lai – Nong Khor | 44.4 | 8% | 11 Apr 2023 | 34 | 13% |
| 4 | Nong Khor – Laem Chabang (phase II) | 14.1 | 3% | 11 Apr 2023 | 12 | 4% |
| | Sub-total (pipelines leased from Treasury Department) | 136 | 26% | | 161 | 61% |
| 5 | EASTW owned pipeline | 387 | 74% | × | 103 | 39% |
| | Total distribution volume | 523 | 100% | | 264 | 100% |
| | Raw water used for internal production of tap water and industrial water | | | | (34) | |
| | Net raw water sales volume | | | | 230 | |

* Pipelines with lease agreements

MCM = million cubic meters

Sources: EASTW

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS*

Unit: Mil. THB

| | Jan-Mar 2023 | -----Year Ended 31 December ----- | | | |
|---|-----------------|-----------------------------------|--------|--------|--------|
| | | 2022 | 2021 | 2020 | 2019 |
| Total operating revenues | 1,125 | 4,298 | 4,641 | 4,218 | 4,701 |
| Earnings before interest and taxes (EBIT) | 256 | 1,079 | 1,442 | 1,138 | 1,472 |
| Earnings before interest, taxes, depreciation, and amortization (EBITDA) | 525 | 2,157 | 2,424 | 2,038 | 2,317 |
| Funds from operations (FFO) | 410 | 1,653 | 1,890 | 1,556 | 1,803 |
| Adjusted interest expense | 83 | 314 | 260 | 256 | 232 |
| Capital expenditures | 723 | 2,833 | 3,078 | 1,609 | 1,527 |
| Total assets | 25,926 | 25,098 | 23,689 | 22,854 | 21,181 |
| Adjusted debt | 12,181 | 11,750 | 10,241 | 8,552 | 7,161 |
| Adjusted equity | 11,719 | 11,568 | 11,427 | 11,069 | 11,014 |
| Adjusted Ratios | | | | | |
| EBITDA margin (%) | 46.64 | 50.18 | 52.24 | 48.31 | 49.28 |
| Pretax return on permanent capital (%) | 4.08 ** | 4.65 | 6.78 | 5.88 | 8.00 |
| EBITDA interest coverage (times) | 6.30 | 6.87 | 9.31 | 7.95 | 9.97 |
| Debt to EBITDA (times) | 5.92 ** | 5.45 | 4.22 | 4.20 | 3.09 |
| FFO to debt (%) | 12.89 ** | 14.07 | 18.45 | 18.19 | 25.18 |
| Debt to capitalization (%) | 50.97 | 50.39 | 47.26 | 43.59 | 39.40 |

* Consolidated financial statements

** Annualized from the trailing 12 months

RELATED CRITERIA

- Corporate Rating Methodology, 15 July 2022
- Key Financial Ratios and Adjustments for Corporate Issuers, 11 January 2022
- Issue Rating Criteria, 15 June 2021

Eastern Water Resources Development and Management PLC (EASTW)

| | |
|--|--------|
| Company Rating: | A |
| Issue Ratings: | |
| EASTW256A: THB1,200 million senior unsecured debentures due 2025 | A |
| EASTW25DA: THB350 million senior unsecured debentures due 2025 | A |
| EASTW275A: THB850 million senior unsecured debentures due 2027 | A |
| EASTW325A: THB750 million senior unsecured debentures due 2032 | A |
| EASTW332A: THB1,000 million senior unsecured debentures due 2033 | A |
| Rating Outlook: | Stable |

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