TRIS RATING
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KHON KAEN SUGAR INDUSTRY PLC

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CORPORATES

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

Company Rating History:

Date	Rating	Outlook/Alert
13/11/13	A	Stable
24/11/06	A-	Stable

Contacts:

Jutatip Chitphromphan

jutatip@trisrating.com

Nauwarut Temwattanangkul

nauwarut@trisrating.com

Sasiporn Vajarodaya

sasiporn@trisrating.com

WWW.TRISRATING.COM

RATIONALE

TRIS Rating affirms the company rating on Khon Kaen Sugar Industry PLC (KSL) and the ratings on its outstanding senior unsecured debentures at "A" with "stable" outlook. The ratings reflect KSL's long track record in the sugar industry, and recent efforts to diversify into other sugar-related businesses. However, the ratings are partially offset by the prolonged slump in sugar prices, the volatility of sugarcane, and the operational risks of KSL's sugar operations in the Lao People's Democratic Republic (Lao PDR) and Cambodia.

KEY RATING CONSIDERATIONS

Strong business profile

KSL's competitive edge is underpinned by its track record in the sugar industry. KSL has the third-largest market share in terms of sugar production. The company covers about 7%-8% of market share by sugar production. KSL's management team has expertise in the sugar industry for over 70 years. KSL's major customers are large-scale food and beverage manufacturers. These industrial users are more concerned about service reliability and product quality due to their specific product requirements. As a result, the company can earn some price premium from offering quality of its products.

Price slump and drought squeeze operating margin

Sugar prices rose in fiscal year (FY) 2017. However, KSL's operating margin, as measured by operating income before depreciation and amortization as a percentage of sales, dropped significantly to 7.2% during FY2017 from around 14% in FY2015-FY2016. A drought reduced the supply of sugar cane and the cost of cane climbed. The severe drought in Thailand cut the amount of KSL's cane crushed to 6.83 million tonnes of cane in the 2016/2017 season, down from 7.61 million tonnes in the 2015/2016 season.

Profits fell in the power segment in FY2017 as well. The falling prices of electricity tariff and fuel adjustment charge (Ft) hurt KSL's operating performance in 2017. Overall, KSL's operating margin rose to 27.2% for the first six months of FY2018, from 24.1% over the same period of FY2017. Production costs for the first six months of FY2018 fell because more cane was available and KSL achieved greater efficiency at its plants.

Global sugar consumption will likely still fall behind production in FY2018 and FY2019, which will continue putting considerable downward pressure on prices. TRIS Rating forecasts KSL's operating margin to be 12% during FY2018. Nonetheless, we believe that the change in the cycle would come after very low sugar prices drove out some supply and production. Thus, the operating margin should recover gradually to 13% in FY2019-FY2021.

Lower contribution from energy segment

TRIS Rating expects the revenue contribution from the energy segment (ethanol and electricity) will decline during FY2018-FY2021. The energy segment will likely make up only 10% of revenue during FY2018, down from around 20% during FY2013-FY2017. The drop was caused mainly by the change of revenue recognition for KSL Green Innovation PLC (KGI), the subsidiary of KSL. As an ethanol producer, KGI was successfully merged with the subsidiaries of Bangchak Corporation PLC (BCP) in October 2017. As a result, KSL must change the revenue recognition of KGI from full consolidation to equity method from FY2018 onwards. The accounting change means Bt2,000 million per year in revenue from the ethanol segment will not be included in KSL's revenue. Based on TRIS Rating base case, we project the company will receive around Bt100-Bt120 million per annum as its share of the profit from the investment in the merged entity.

Improving financial leverage

We expect KSL's financial leverage will improve gradually during FY2018-FY2021. Total debt to capitalization ratio will decline, ranging between 47%-53% during FY2018-FY2021. Capital expenditure will likely fall in the range of Bt400-Bt1,200 million per year in FY2018-FY2021, compared with Bt2,000-Bt3,000 million per year during FY2016-FY2017. KSL plans to spend Bt800 million to expand its cane capacity in Loei province and Bt400 million in maintenance expenditure during FY2018.

We see KSL's cash flow protection, as measured by the funds from operations (FFO) to total debt ratio, will improve gradually. The ratio is forecast to be 7.4%-11.8% during FY2018-FY2021. Cash flow protection and the earnings before interest, tax, depreciation, and amortization (EBITDA) interest coverage ratio move in the same pattern with sugar prices. The EBITDA interest coverage ratio could move in the range of 3-5 times during FY2018-FY2021 once sugar prices recover.

Sound liquidity

Over the next 12 months, we expect KSL's liquidity to be adequate. Our base case assumes EBITDA will increase to Bt2,500-Bt2,900 million in FY2018-F2021 following a gradual recovery in sugar prices. In addition, the office of the cane and sugar fund (OCSF) will pay KSL around Bt300-Bt350 million per year as compensation for sugar production from revenue sharing. Cash and cash equivalents were Bt210 million, plus unused credit facilities of Bt18,261 million at the end of April 2018. KSL has scheduled debt repayments of Bt4,000-Bt5,000 million per year during FY2018-FY2021.

RATING OUTLOOK

The "stable" outlook reflects TRIS Rating's expectation that KSL will maintain its competitive position in the Thai sugar industry. The revenue sharing system of the Thai sugar industry and revenue contribution from its power business will alleviate the volatility in its sugar production business.

RATING SENSITIVITIES

KSL's rating upside is limited in the short term as long as sugar prices stay low. In contrast, KSL's ratings could be revised downward, if profitability and earnings fall short of expectations. The prolonged slump in raw sugar prices worldwide is a negative factor for the ratings as the low prices will pressure KSL's financial performance. Any aggressive, debt-funded investment, and a drop in cash flow protection would impact the credit ratings.

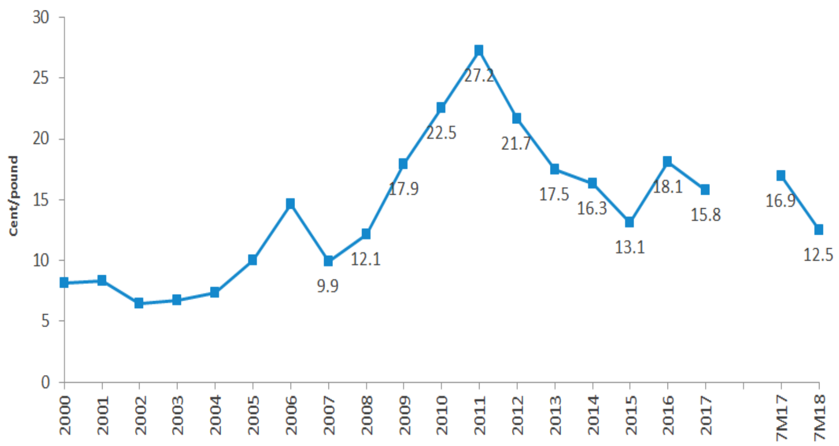
COMPANY OVERVIEW

KSL is one of the leading sugar producers in Thailand, established in 1945 by the Chinthammit family and associates. As of April 2018, the Chinthammit family collectively held 66% of the company's shares. The company owns and operates five sugar plants in Thailand, with a combined cane crushing capacity of 110,000 cane tonnes per day as of April 2018. KSL procured 11.03 million tonnes of sugarcane in the 2017/2018 crushing period and produced 1.20 million tonnes of sugar. KSL's sugar production in the 2017/2018 growing season ranked the third in the industry, with a market share of 8.2%. KSL trailed the Mitr Phol Group (18.5%), the Thai Roong Ruang Group (14.5%).

KGI, a subsidiary of KSL, was merged with BBP Holding Co., Ltd. (BBH), a subsidiary of BCP. The merged operation under BBGI PLC (BBGI) represents a business alliance for bio-based products. BCP holds 60% of BBGI; the remaining 40% is held by KSL. The merger means BBGI will become Thailand's largest producer of bio-fuel. The merger was completed on 31 October 2017. BBGI has planned an initial public offering (IPO) during FY2018-FY2019 to secure the funds it needs for business expansion.

KEY OPERTING PERFORMANCE

Chart 1: Raw Sugar Prices 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: Million tonnes

Sugar Producer	Growing Season				
	2013/ 2014	2014/ 2015	2015/ 2016	2016/ 2017	2017/ 2018
Mitr Phol	2.30	2.30	1.96	1.98	2.73
Thai Roong Ruang	1.75	1.60	1.37	1.42	2.13
KSL Group	0.91	0.91	0.77	0.72	1.20
Thai Ekkalak	1.06	0.99	0.72	0.94	1.19
Wangkanai	0.70	0.56	0.51	0.39	0.79
Banpong	0.46	0.44	0.44	0.44	0.52
Kumpawapee	0.37	0.40	0.30	0.28	0.41
Others	3.78	4.10	3.71	3.86	5.74
Total	**11.33**	**11.30**	**9.78**	**10.03**	**14.71**

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

Table 2: KSL's Revenue Breakdown by Business

Unit: %

Product	2014	2015	2016	2017	Nov 17-Apr 18
Sugar sales					
- Thailand	68.8	69.0	74.9	73.2	79.8
- Laos &	1.5	1.9	5.3	3.9	1.7
Ethanol and fertilizer sales	12.5	13.3	11.9	13.4	-
Electricity sales	5.9	5.4	4.8	4.8	8.1
Service and others	11.3	10.4	3.1	4.7	10.4
Total sales	**100**	**100**	**100**	**100**	**100**

Source: KSL

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS*

Unit: Bt million

	Nov 2017-Apr 2018	-------------Year Ended 31 October ------------ 2017	2016	2015	2014
Sales and service revenues	6,831	15,623	16,911	17,475	19,185
Gross interest expense	314	664	706	813	807
Net income from operations	829	371	1,435	861	1,610
Funds from operations (FFO)	1,391	473	1,510	1,947	2,957
Capital expenditures	855	3,133	1,981	646	2,687
Total assets	52,961	42,991	38,375	36,640	40,134
Total debts	29,619	21,700	18,839	21,222	22,026
Shareholders' equity	18,571	18,092	16,650	13,666	14,833
Operating income before depreciation and amortization as % of sales	27.18	7.21	13.71	13.89	18.04
Pretax return on permanent capital (%)	1.58 **	2.71	6.53	4.71	7.72
Earnings before interest, tax, depreciation, and amortization (EBITDA) interest coverage (times)	6.79	3.31	5.02	3.47	4.73
FFO/total debt (%)	(0.64) **	2.20	8.04	9.19	13.46
Total debt/capitalization (%)	61.45	54.58	53.10	60.85	59.76

Note: All ratios have been adjusted by operating leases
* *Consolidated financial statements*
** *Annualized with trailing 12 months*

Khon Kaen Sugar Industry PLC (KSL)

Company Rating:	A
Issue Ratings:	
KSL189A: Bt1,000 million senior unsecured debentures due 2018	A
KSL192A: Bt1,000 million senior unsecured debentures due 2019	A
KSL198A: Bt1,000 million senior unsecured debentures due 2019	A
KSL199A: Bt1,000 million senior unsecured debentures due 2019	A
KSL202A: Bt1,000 million senior unsecured debentures due 2020	A
KSL27DA: Bt2,000 million senior unsecured debentures due 2027	A
Rating Outlook:	Stable

TRIS Rating Co., Ltd.
Silom Complex Building, 24th Floor, 191 Silom Road, Bangkok 10500, Thailand Tel: 0-2098-3000