TRIS RATING
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TPI POLENE POWER PLC

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CORPORATES

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

Last Review Date: 17/07/19

Company Rating History:

Date	Rating	Outlook/Alert
10/04/19	BBB+	Positive
17/09/18	BBB+	Stable

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RATIONALE

TRIS Rating affirms the company rating on TPI Polene Power PLC (TPIPP) and the ratings on TPIPP's existing senior unsecured debentures at "BBB+". At the same time, TRIS Rating revises the outlook on TPIPP to "stable" from "positive", following a change in the rating outlook on its parent company, TPI Polene PLC (TPIPL). The outlook revision reflects our expectation of hefty capital spending that will keep the parent company's financial leverage to be in a high level over the medium term.

TRIS Rating also assigns the rating of "BBB+" on TPIPP's newly proposed issue of up to Bt6 billion in senior unsecured debentures. The company intends to use major part of the proceeds to fund the purchase of land in Songkhla province.

The ratings continue to reflect TPIPP's robust cash flows from the power purchase agreements (PPAs) with the Electricity Generating Authority of Thailand (EGAT), its high profitability from adders, competitive fuel costs, and strong financial profile. However, the ratings are offset by the relatively high operational risks of refuse-derived fuel (RDF) power plants and our concerns on large debt-funded investments in the Special Economic Zone (SEZ) development project in the Southern part of Thailand.

KEY RATING CONSIDERATIONS

Rating capped by the parent company's rating

TPIPP's ratings are capped by TPIPL's ratings at "BBB+" as TPIPP is a core subsidiary of TPIPL (rated "BBB+/Stable" by TRIS Rating). On a stand-alone basis, TPIPP's company rating is assigned at "A", suggesting a stronger credit profile than TPIPL.

The capped ratings reflect a strong parent-subsidiary relationship between the two entities. TPIPL remains the ultimate shareholder, holding a stake of about 70.24% in the company. TPIPL's top management team also involves in TPIPP's board of directors and has significant influence over TPIPP's business strategies and financial policies.

TRIS Rating expects TPIPP to play a crucial role in supporting the ratings on the TPIPL's group. The company will continue to be the largest cash flow contributor, generating about 70% of the group's earnings before interest, tax, depreciation, and amortization (EBITDA).

The ratings also take into account a significant degree of business integration between TPIPP and its parent company. The interdependence causes operational constraints on TPIPP and exposes the company to TPIPL's credit risk and the cyclicality of the cement business. Additionally, since TPIPL is a power buyer and the sole supplier of waste heat to TPIPP, adverse changes in TPIPL's cement plant operations will likely cause fluctuations in its power demand and supply of waste heat, which in turn will affect the operations of TPIPP's power plants.

Robust cash flow from EGAT PPAs

TRIS Rating believes that TPIPP's solid cash flow generation will continue, supported by the long-term PPAs with EGAT (rated "AAA/Stable" by TRIS Rating). Under the terms of PPAs, TPIPP will receive recurring cash flow as long as its power plants are able to generate and distribute electricity to the off-taker. TPIPP's three PPAs, totaling 163 megawatts (MW), come with a tariff adder rate of Bt3.50 per kilowatt-hour (kWh) on top of base tariff rate of approximately Bt3 per kWh for seven years, markedly lifting the company's profit margin to a high level.

We note that steady cash flows from the PPAs will step down during 2022-2023 since the adders of the first two PPAs will expire in January and August 2022. These two PPAs have a combined contracted capacity of 73 MW. The adder of the last PPA (90 MW) will end in April 2025.

Competitive fuel costs

TPIPP's advantages are underpinned by the low costs of the RDF and waste heat. The cost of RDF is relatively low as it can be produced from landfill waste and municipal solid waste (MSW). Waste heat, a by-product from cement production, is another advantage exclusive to TPIPP due to the proximity of its power plants to its parent's cement plants. The waste heat supply is unstable and it moves in tandem with the utilization rate of TPIPL's cement plants.

TRIS Rating expects TPIPP's fuel costs will remain competitive. The potential for rising feedstock price is partly mitigated by the improving efficiency of its power plants. Currently, TPIPP can feed and burn MSW directly in some boilers of the RDF-fired power plants, helping saving conversion cost. The proportion of MSW grew to 31% in 2019 from 19% in 2018. The balance comes from pre-sorted landfill waste, which is much more costly than MSW. Once the three new boilers are installed completely within 2020, we expect the proportion of MSW in the fuel mix to increase further, reducing TPIPP's overall fuel costs.

High operational risks of RDF power plants

RDF-fired power plants are more complex than conventional fossil-fuel plants, given the varying quality of feedstock. RDF-fired power plants have greater potential for operational outages than power plants with stable quality of fuels. With low plant stability, large and continuous expenditures for plant improvement and maintenance will be required to sustain plant efficiency. However, we view the high operational risk is alleviated by TPIPP's long track record in operating RDF-fired power plants and measures to prevent unplanned shutdowns.

Risk exposure from land procurement

The SEZ project has been initiated by the government with the aim to develop the economy in the strategic region of Thailand. Early this year, the Cabinet agreed in principle to establish the SEZ in Chana district, Songkhla province. The development, covering 16,700 rai of land, would include deep-sea ports, industrial estates, and power plants with 3,700 MW of capacity.

TPIPP is eager to take part in the SEZ project. Currently, the company aims to develop a 1,700-MW gas-fired power plant in the SEZ. In preparing the proposal and getting an early foothold for the project, the company has gradually acquired land in those areas since the late of 2018. TPIPP has entered into several land purchase agreements for total 16,700 rai of land. Total land cost is about Bt12 billion. At the end of December 2019, the company has paid Bt5.6 billion for land and plans to pay for the remainder during 2020-2021.

We view that the early land procurement exposes TPIPP to several risks. The project commencement is still uncertain. The early decision may put the company under pressures from a risk of project delay, possible changes in the government's policy, and the possibility of opposition from local communities. Further, the project may take years before bid opening. With an unknown project timeline, the company is likely to carry the lands without any return for an extended period. However, we believe TPIPP's financial strength can shoulder this burden. The company's risks should be confined as we believe that TPIPP will not make any further investment in the SEZ project unless it obtains official agreement from the government, such as the new PPA.

In case that TPIPP wins the bid to develop the SEZ project, its financial leverage will rise substantially. TPIPP will need to spend over Bt100 billion for the first phase of the project development, including the construction of the power plant worth Bt70-80 billion. TPIPP's large debt raising will significantly deteriorate the group's financial profile which would cause downward ratings of the parent company and TPIPP. However, we believe TPIPP would need to seek capable partners or come up with a well-suited financing scheme to avert an overleveraged structure.

Expected EBITDA to peak in 2021

TPIPP's financial performance in 2019 continues to improve, driven by increasing power outputs. TPIPP's power outputs in 2019 totaled 1,957 gigawatt hours (GWh), rising from 1,248 GWh in 2018. The company's EBITDA grew by 31.9% to Bt5.56 billion from Bt4.22 billion over the same period last year. The EBITDA margin remained high at 52.1%.

However, the performance of the new 150-MW coal power plant, which sells electricity to TPIPL, still falls short of its target. The coal power plant cannot run at the target level since the load demand is tied to power consumption of TPIPL's cement factories. The cement production lines intensively operate during the off-peak period due to the much lower tariff of electricity. But the cement production will drop sharply during the on-peak period to reduce costs. This results in a wild swing in TPIPP's power generation. However, we expect the technical issues will be resolved by the revision of PPA, which allows TPIPL to pay lower tariff during the on-peak period.

In our base-case forecast, we expect TPIPP's cash flow to improve further. The utilization rates of the RDF-fired power plants will improve following the complete installation of new boilers in 2020. EBITDA will reach Bt6 billion in 2020 and Bt6.5 billion in 2021 before dropping to Bt5.8 billion in 2022 due to the adder expiration. EBITDA margin is expected to decline due to a larger contribution from the coal-fired power plant. However, overall EBITDA margin should remain high in a range of 48%-52%.

Strong capital structure

We expect TPIPP to maintain its strong financial profile. Currently, the company plans to participate in bidding for a number of projects, including two waste-to-energy (WTE) power plants (9.9 MW each) in Songkhla and Nakhon Ratchasima provinces, new power plants under the Power Development Plan (PDP2018), and acquisitions of PPAs from not-yet-operating projects. In our base-case forecast for 2020-2022, capital expenditures (CAPEX) is projected to total Bt16.7 billion, mainly including land procurement of about Bt6.5 billion and pending payments for the three boilers and new RDF sorting line of Bt1.9 billion. We also add on CAPEX of Bt8 billion for potential new investments in WTE power plants.

As a result, the debt to capitalization ratio of TPIPP will stay between 30%-35% and its debt to EBITDA ratio will be maintained at 2-3 times. These financial ratios indicate a comfortable level of financial leverage. However, we highlight the company is in a period of seeking growth, which means the larger-than-expected investments remain possible.

In the base-case scenario, we do not incorporate the investment outlays in the first phase of the SEZ project, given unforeseeable project timeline and financing structure.

BASE CASE ASSUMPTIONS

- Total power output to increase to 2.35 GWh per annum during 2020-2022.
- Total operating revenues to increase to Bt11-Bt12 billion per annum during 2020-2022.
- EBITDA margin to hold at around 50% during 2020-2022.
- Total capital spending of about Bt16.7 billion during 2020 and 2022.
- Dividend per share of about Bt0.30-Bt0.40 during 2020 and 2022.

RATING OUTLOOK

The "stable" outlook of TPIPP follows the revision of TPIPL's outlook. TRIS Rating expects that TPIPP's power plant operations will continue to render solid cash flows over the long term. TPIPP's status as a core subsidiary of TPIPL is likely remain. Therefore, any change in TPIPL's ratings will affect TPIPP's ratings.

RATING SENSITIVITIES

The rating upgrade is limited due to the prospect of large investments in new power projects. Conversely, a downgrade of ratings could occur if TPIPP's operating performance is weaker-than-expected or if the company makes excessive debt-financed investments and result in a significant surge of the group's consolidated outstanding debt. The ratings or outlook could also be revised downward if TRIS Rating downgrades TPIPL's ratings.

COMPANY OVERVIEW

Established in 1991, TPIPP is the largest WTE power producer in Thailand. The company commenced operation of its first waste heat recovery power plant in 2009 to support TPIPL's cement production. TPIPP later opened two RDF-fired power plants, selling the electricity to EGAT in 2015. TPIPP was listed on the Stock Exchange of Thailand (SET) in April 2017. The company's business includes the generation and sale of electricity from the RDF and waste heat recovery power plants as well as the petrol and gas service stations.

The company currently owns and operates seven power plants, mainly using RDF, waste heat, and coal as fuels. The total installed capacity is 440 MW. All power plants are located in Saraburi province, proximate to TPIPL's cement plants. The company distributes electricity to two utility off-takers, EGAT and TPIPL. TPIPP carries three PPAs with EGAT, permitting the company to sell a capacity of 163 MW with an adder of Bt3.5 per kWh on top of the base tariff of approximately Bt3 per kWh.

In 2019, total sales of TPIPP came in at Bt10.6 billion. The power business accounted for over 90% of total sales. Revenues received from EGAT and TPIPL accounted for 73% and 20% of its total revenue, respectively.

KEY OPERATING PERFORMANCE

Table 1: Power Project Portfolio as of Dec 2019

Project/Country	Hold (%)	Status	Installed Capacity (MW)	Contracted Capacity with EGAT (MW)	Off-taker	Tariff Scheme	Commercial Operating date
Thailand							
WH-40 MW	100	Operating	40		TPIPL		Jun 2009
RDF-20 MW	100	Operating	20	18	EGAT	Adder Bt3.5	Jan 2015
RDF-60 MW	100	Operating	60	55	EGAT	Adder Bt3.5	Aug 2015
WH-30 MW	100	Operating	30	90*	EGAT	Adder Bt3.5	Jan 2016
RDF-70 MW	100	Operating	70	90*	EGAT	Adder Bt3.5	Apr 2018
Coal/RDF-70 MW	100	Operating	70**		TPIPL		Aug 2018
Coal-150 MW	100	Operating	150		TPIPL		Jan 2019
			440	**163**			

Source: TPIPP
** WH-30 MW and RDF-70 MW started selling power output to EGAT in Apr 2018 under the same PPA of 90 MW.*
*** Approved capacity of 40 MW*

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS*

Unit: Bt million

	------------------------ Year Ended 31 December ------------------				
	2019	**2018**	**2017**	**2016**	**2015**
Total operating revenues	10,692	7,704	4,894	4,407	2,692
Earnings before interest and taxes (EBIT)	4,759	3,736	2,500	1,960	986
Earnings before interest, taxes, depreciation, and amortization (EBITDA)	5,566	4,217	2,867	2,331	1,313
Funds from operations (FFO)	5,218	4,018	2,681	2,129	1,199
Adjusted interest expense	246	39	110	209	220
Capital expenditures	6,877	4,940	4,982	3,893	1,658
Total assets	37,853	31,541	27,567	18,169	12,674
Adjusted debt	6,123	1,225	0	7,145	1,558
Adjusted equity	27,110	25,048	24,214	8,321	9,045
Adjusted Ratios					
EBITDA margin (%)	52.1	54.7	58.6	52.9	48.8
Pretax return on permanent capital (%)	14.5	13.8	12.4	14.8	9.2
EBITDA interest coverage (times)	22.6	108.0	26.0	11.2	6.0
Debt to EBITDA (times)	1.1	0.3	0.0	3.1	1.2
FFO to debt (%)	85.2	328.1	N.M.	29.8	76.9
Debt to capitalization (%)	18.4	4.7	0.0	46.2	14.7

** Consolidated financial statements*
N.M. Not meaningful

RELATED CRITERIA

- Rating Methodology – Corporate, 26 July 2019
- Key Financial Ratios and Adjustments, 5 September 2018
- Group Rating Methodology, 10 July 2015

TPI Polene Power PLC (TPIPP)

Company Rating:	BBB+
Issue Ratings:	
TPIPP21NA : Bt4,000 million senior unsecured debentures due 2021	BBB+
TPIPP22NA : Bt4,000 million senior unsecured debentures due 2022	BBB+
Up to Bt6,000 million senior unsecured debentures due within 5 years	BBB+
Rating Outlook:	Stable

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