

# PTT EXPLORATION AND PRODUCTION PLC

No. 32/2018

29 March 2018

## CORPORATES

<b>Company Rating:</b>	AAA
<b>Issue Ratings:</b>	
Senior unsecured	AAA
Hybrid	AA
<b>Outlook:</b>	Stable

### Company Rating History:

Date	Rating	Outlook/Alert
16/03/06	AAA	Stable
12/07/04	AA+	Positive
28/11/01	AA+	
21/11/00	AA	

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## RATIONALE

TRIS Rating affirms the company rating of PTT Exploration and Production PLC (PTTEP) and the ratings of PTTEP's senior unsecured debentures at "AAA". TRIS Rating also affirms the rating of "AA" to PTTEP's subordinated capital debentures. The two notches below the company rating reflect the deferability and subordinated nature of the subordinated capital debentures.

PTTEP's ratings reflect the company's leading position in the petroleum exploration and production (E&P) industry in Thailand, low market risk due to long-term gas sale agreements with PTT PLC (PTT), low production cost from legacy assets, conservative financial policy, and strong financial profile. The decline in proved reserves increases the potential of acquiring additional reserves, and the execution risk PTTEP faces in its overseas operations remains a rating concern.

## KEY RATING CONSIDERATIONS

### Leading position in the Thai E&P

PTTEP is the petroleum E&P arm of PTT, the Thai-national oil and gas company. PTT is a major shareholder of PTTEP, holding about 65.3%. Both PTT and PTTEP are state enterprises. PTT is also a major customer, accounting for about 87% of PTTEP's sales. Therefore, PTTEP faces very little credit risk from its major customer. Currently, PTT is the sole natural gas supplier in Thailand. The company's business strategies fit with PTT's strategic move to secure itself as the nation's energy source.

As the E&P arm of PTT and the Thai government, PTTEP can participate in high potential petroleum projects in Thailand and abroad.

### GSAs with PTT strengthen business profile

About 70% of PTTEP's sales volume is natural gas, with a long-term agreement with PTT. Gas price is formulated through Gas Sales Agreements (GSAs). All of the GSAs are long-term contracts on a take-or-pay basis. A buyer has to take the minimum annual contracted quantity of natural gas indicated in the GSA or pay the equivalent amount. This contractual arrangement partly secures PTTEP's sales volume.

The selling price of natural gas helps stabilize PTTEP's average selling price. The pricing formulas stipulated in the GSAs limit PTTEP's exposure to oil price fluctuations. About 30%-50% of gas pricing is indexed to fuel oil prices, with a lag time of three months to one year. In addition, the pricing formula includes adjustments for inflation and foreign exchange rate fluctuations.

### Low production cost

PTTEP has demonstrated its ability to maintain low production cost during the low oil price environment. Since the second half of 2014, PTTEP has been able to maintain its earnings before interest, tax, depreciation, and amortization (EBITDA) margin of over 70%. The lifting cost (cost to produce petroleum for one barrel) was well managed at about US\$4-US\$5 per barrel of oil equivalent (boe). In addition, the cost reduction program helped maintain unit cash cost at about US\$14 per boe in 2017.

### Reserves decline but are expected to improve

At the end of 2017, the company's proved reserves declined to 631 million barrels of oil equivalent (mmboe), compared with 695 mmboe at the end of 2016. These reserves indicate a reserve life of about five years.

However, PTTEP held large petroleum resources (proved and probable reserves plus contingent resources) of about 4,800 mmboe at the end of 2017. This amount has a potential to convert resources to proved reserves, assuming ability and a sound economic environment. Current projects include the Mozambique Rovuma Offshore Area 1, Southwest Vietnam, Algeria HBR and Ubon (Contract 4). If the company finalizes its decision to develop these four projects, PTTEP will gain one to two years of proved reserves, based on the 2017 production.

### Potential for Bongkot bidding and mergers & acquisition

PTTEP will participate in bidding on the Bongkot and Erawan projects. The winner is expected to be announced by the end of 2018. TRIS Rating forecasts that PTTEP's production volume may increase by at least 82,000 barrels of oil equivalent per day (boed), if PTTEP win a bid for Bongkot and Erawan projects with its current working interest. However, if PTTEP is not selected, the company might have to focus on merger and acquisition (M&A) activities, especially towards producing assets with the aim of increasing production levels and increasing reserves.

### Profitability is still healthy as a result of cost saving efforts

An increase in oil prices in 2017 helped increase the company's revenue despite a drop in sales volume. PTTEP's revenue increased by 2% from US\$4,190 million to US\$4,281 million in 2017. The operating margin (operating income before depreciation and amortization as a percentage of sales) was healthy at 70.7%. The company's EBITDA improved from US\$2,996 million in 2016 to US\$3,183 million. This level of EBITDA could cover the outstanding debt of US\$2,907 million. TRIS Rating forecasts that the company's EBITDA will be in the range of US\$3,400-US\$3,700 million per year during 2018-2020. This is based on an oil price assumption of US\$50-US\$60 per barrel. In addition, sales volume should increase about 17,000 boed in 2018, if the company increases its stake in the Bongkot project by 22%.

### Very strong liquidity profile

PTTEP's liquidity is very strong. At the end of 2017, its source of funds comprised cash on hand of US\$4,468 million and undrawn credit facilities of US\$895 million, of which US\$612 million was a committed credit line. Its funds from operations (FFO) over the next 12 months are expected to be around US\$3,000 million. The company's total debt due over the next 12 months will be only US\$406 million. The company's planned capital expenditures over the next 12 months will be around US\$1,800 million. In addition the company has budgeted about US\$750 million (before tax) to acquire 22% interest in Bongkot project. The company's cash on hand plus the expected FFO could cover the company's expenditures and debt repayment.

### RATING OUTLOOK

The "stable" outlook reflects TRIS Rating's expectation that PTTEP will be able to maintain its strong financial position amid challenging market conditions. The ability to rationalize capital expenditure and ample liquidity will help PTTEP weather the downturn in the petroleum industry.

### RATING SENSITIVITIES

A credit downside may arise if crude oil prices stay below US\$30 per barrel for a prolonged period, which would impact the company's ability to generate cash, and if PTTEP's financial leverage increases significantly due to any large debt-funded acquisitions.

### COMPANY OVERVIEW

PTTEP is the leading petroleum E&P company in Thailand. The company was established in 1985 to hold petroleum concession rights on behalf of the Thai government. As of February 2018, PTT, the national oil and gas company, held a 65.3% shareholding in PTTEP. Both PTT and PTTEP are state enterprises. As of December 2017, the company had 36 E&P projects across 10 countries. Twenty three projects are in the production phase and the remaining 13 projects are in the exploration phase.

At the end of 2017, PTTEP owned proved reserves of 631 mmboe. About 75% of proved reserves were natural gas and the remaining 25% were crude oil and condensate. PTTEP is the largest petroleum producer in Thailand, with a production rate of 347,507 boed in 2017, accounting for about 29% of Thailand's total petroleum supply. The company's revenue of US\$4,281 million came from Thailand (73.7%), South East Asia, mainly Myanmar (19.9%), Australia (5.2%), and the rest of the world (1.2%).

**KEY OPERATING PERFORMANCE**

	----- Year Ended 31 December -----				
	2017	2016	2015	2014	2013
Proven reserves (mmboe)	631	695	738	777	846
Yearly production (mmboe)	127	135	136	131	120
Reserve life (years)	5	5	5	6	7
Five-year reserve replacement ratio (times)	0.6	0.6	0.5	0.5	0.8
Lifting costs (US\$/boe)	4.2	4.2	4.6	5.3	4.9
Average sales volume (boed)	299,206	319,521	322,167	312,569	292,629
Average selling price (US\$/boe)	39.20	35.91	45.29	63.71	65.58

*mmboe* = million barrels of oil equivalent

*boe* = barrel of oil equivalent

*boed* = barrel of oil equivalent per day

**FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS\***

Unit: US\$ million

	----- Year Ended 31 December -----				
	2017	2016	2015	2014	2013
Revenue	4,281	4,190	5,287	7,319	7,172
Gross interest expense	226	234	252	259	201
Net income from operations	1,101	387	597	1,724	1,936
Funds from operations (FFO)	2,666	2,352	2,987	4,245	3,814
Earnings before interest, tax, depreciation, and amortization (EBITDA)	3,183	2,996	4,231	5,914	5,369
Capital expenditures	1,332	998	1,734	2,051	2,633
Total assets	19,220	18,891	19,642	23,271	21,572
Total debts	2,907	2,832	3,005	4,229	4,023
Shareholders' equity	11,517	11,386	11,328	12,548	11,719
Operating income before depreciation and amortization as % of sales	70.7	71.4	74.2	74.5	71.7
Pretax return on permanent capital (%)	10.5	6.4	8.6	18.8	24.0
Earnings before interest, tax, depreciation, and amortization (EBITDA) interest coverage (times)	12.4	11.0	14.5	21.0	24.8
FFO/total debt (%)	74.5	66.7	79.9	86.1	89.9
Total debt/capitalization (%)	24.6	24.5	25.7	29.2	26.9

Note: All ratios have been adjusted by operating leases and subordinated capital debentures (50% of the outstanding is treated as debts and the rest is treated as equity).

\* Consolidated financial statements

**PTT Exploration and Production PLC (PTTEP)**

<b>Company Rating:</b>	AAA
<b>Issue Ratings:</b>	
PTTEP195A: Bt5,000 million senior unsecured debentures due 2019	AAA
PTTEP196A: Bt8,200 million senior unsecured debentures due 2019	AAA
PTTEP296A: Bt11,400 million senior unsecured debentures due 2029	AAA
PTTEP12PA: Bt5,000 million subordinated capital debentures	AA
<b>Rating Outlook:</b>	Stable

**TRIS Rating Co., Ltd.**

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