

EAST COAST FURNITECH PLC

No. 125/2022
27 July 2022

CORPORATES

Company Rating: BB
Outlook: Stable

Last Review Date: 30/07/21

Company Rating History:

Date	Rating	Outlook/Alert
30/07/21	BB+	Stable
23/07/20	BB+	Negative
25/07/18	BB+	Stable
19/06/17	BB	Stable

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RATIONALE

TRIS Rating downgrades the company rating on East Coast Furnitech PLC (ECF) to “BB” from “BB+”. The downgrade reflects increasing uncertainties for the company to secure project financing for the Minbu solar power project in Myanmar after the central bank of Myanmar ordered suspension of foreign loan repayments. The downgrade also reflects our anticipation that ECF’s high financial leverage is likely to continue, considering from the higher possibility of further postponement of the phase 3-4 of the Minbu project.

The rating continues to reflect ECF’s adequate competitive strength in the furniture market and established distribution channels through modern-trade retailers in Thailand and overseas markets.

KEY RATING CONSIDERATIONS

Heightened investment risk of the Minbu project

The Minbu project is expected to face difficulties in seeking project financing from financial institutions. The central bank of Myanmar’s directive on 13 July 2022 for local companies to suspend foreign loan repayments raises our concerns on the possibilities of securing project financing to fund investments in Myanmar. Our concerns encompass other potential operational impacts, including the currency of received revenue, payments for contractors or suppliers, and foreign remittances to Thailand.

Development of the 50-megawatt (MW) Minbu phase 2 continues to be delayed. To date, project financing has not been granted as the lender’s project assessment was interrupted by the Coronavirus Disease 2019 (COVID-19) pandemic and internal conflicts in Myanmar. Currently, the project construction was preliminary funded by loans from the project owners.

We view the likelihood of securing project loan from foreign financial institutions for the Minbu project will prove more challenging, considering Myanmar’s current political situation and the Myanmar government’s latest measure to control foreign outflows. Without external financing, the developments of the Minbu project phase 3 and 4 are likely to be postponed. The Minbu project is significant to ECF as the project is the company’s largest investment, worth THB908 million in total at the end of March 2022, representing 23% of ECF’s total assets.

Adequate competitive strength in furniture market

ECF’s business strength is underpinned by its established market position as a medium-sized furniture manufacturer in Thailand. The company is considered an original equipment manufacturer (OEM) since the majority of its furniture sales are made-to-order products. We view ECF’s competitive strength as adequate to maintain its market position. The company benefits from own production facilities and larger economies of scale, compared with most furniture manufacturers.

Nevertheless, its business profile is constrained by price-driven competition, and limited pricing power in the furniture market as most products are simple knockdown furniture targeted at the low- to medium-priced segments.

Established distribution channels in modern-trade retailers

ECF has two core distribution channels, comprising exports and Thai modern-trade retailers. Most of ECF’s export customers are leading furniture and

modern trade retailers in Japan. The company has distributed through these two channels for long periods, and we consider them to be an essential factor supporting sales growth over the past several years. In 2021, the export market accounted for 64% of ECF's total furniture sales, while Thai modern trade made up about 32% of the total.

Customer bases increasingly diversified

ECF's business profile benefited from improved revenue geographical diversity with less concentration risk in the Japanese market. Furniture orders from the United States and India have grown noticeably in 2021, contributing about 10% and 8.7% of the total, respectively. The sales proportion from Japan reduced approximately 40% of total sales in 2021 while Thai market continues to deliver about 39% of total revenue.

With various market bases, we view that ECF's furniture performance is likely to be more stable. ECF's Indian market shows growth potential as its key customers are large online retailers, which should benefit from the uptick in online shopping.

Sustained performance in furniture segment

We expect ECF to be able to keep its revenue at around THB1.6 billion per annum over the next 2-3 years. ECF has noticeably benefited from the work-from-home trend with its revenue climbing to a peak of THB1.6 billion in 2021, up by 13% year-on-year (y-o-y). The company's furniture export volumes are likely to contract this year in line with the global economic. However, this is likely to be counterbalanced by benefits resulting from depreciation of the Thai baht against the dollar and an expected recovery of demand for renovations in the Thai hotel and leisure sector, backed by the return of significant numbers of tourists.

However, rising particleboard prices, coupled with higher labor costs and energy prices, continue to weigh down the company's profitability. The company's earnings before interest, taxes, depreciation, and amortization (EBITDA) margin dropped slightly to 12.6% in 2021 and 12.3% in the first quarter of 2022. We expect its EBITDA margin from the furniture business will decline slightly but remain in the 12.0%-12.5% range during 2022-2024, considering the company's ongoing productivity improvements and cost-saving efforts.

Higher-than-expected financial leverage

ECF's financial profile is weaker than our previous forecasts as the Minbu project cannot deliver cash flow to help reduce debt as planned. All cash flows from the phase 1 project are used to support construction of the remaining phases. The company's total debts also increased as the company provided shareholder's loan to support the construction of the Minbu project while awaiting loan approvals. The net debt to EBITDA ratio rose to 10.5 times in the first quarter of 2022, from 8.8 times in 2021.

We forecast ECF's financial leverage will remain at high level, as seen from the company's capital spending plan and our expectation of no dividend payments from the Minbu project. We expect ECF's net debt to EBITDA ratio to stay above 10 times during 2022-2023. The ratio of funds from operations (FFO) to net debt will likely fall below 5%. In our view, the chance of the company to restore its financial profile will largely depends on the completion and fully operation of all phases of the Minbu project.

Liquidity continues to be tight

ECF's sources of funds are expected to be almost equal to its uses of funds over the next 12 months. The sources of funds consist of cash on hand of THB35 million as of March 2022, estimated FFO of THB40-THB50 million, and proceeds from a bond issued in June 2022 totaling about THB850 million. The uses of funds will include bond repayments of THB512.4 million, bill of exchange and loan repayments of THB406.1 billion, and dividends of THB15 million. Its planned capital expenditure of about THB200 million over the next 12 months is likely to be supported by external financing.

Capital structure

At the end of March 2022, ECF had THB2.14 billion of debt, including around THB1.83 billion of priority debt. As its priority debt ratio of about 85.6% is higher than the threshold of 50%, we view that ECF's unsecured creditors are significantly disadvantaged with respect to the priority of claims against ECF's assets.

BASE-CASE ASSUMPTIONS

- Revenue to be around THB1.6 billion per annum during 2022-2024.
- Shared profits from the Minbu investments to rise to THB68 million in 2023 and to remain flat thereafter.
- EBITDA margin, excluding cash flow from the Minbu project, to stay between 12.0%-12.5% during 2022-2024.
- Capital expenditure to be THB233 million in 2022 and about THB80 million per year in 2023-2024.
- Dividend payout ratio to be 30% during 2022-2024.

RATING OUTLOOK

The “stable” outlook reflects our expectation that the company’s furniture business will maintain its operating performance. The Minbu phase 2 project will be up and run within 2023 with no dividend receipt until the project is fully completed.

RATING SENSITIVITIES

A rating upgrade may occur if the company can secure adequate funds to complete the Minbu project and we see that political risk and capital controls in Myanmar are not likely to have a significant effect on the project. An upgrade may also occur if the net debt to EBITDA ratio of ECF falls below 8 times for a sustained period.

A further rating downgrade could occur if ECF’s financial position deteriorates significantly further. This could result from weakening performance in the furniture business, additional debt-financed investments, and failure of the Minbu project.

COMPANY OVERVIEW

ECF engages in the manufacture and distribution of home furniture in Thailand. The company owns two factories in Rayong province, focusing on producing knockdown furniture and rubber wood furniture. Revenue from selling furniture contributes over 90% of its total revenue; the remainder is derived from selling decorative foil paper and dried rubber wood. ECF has been listed on the Market for Alternative Investment (MAI) since 2013. The Suksawad family is the main shareholder, holding approximately 50% of the company’s outstanding shares in March 2022.

ECF distributes its furniture products through two main channels, including made-to-order for export and Thai modern trade. Almost all made-to-order furniture is exported to leading furnishing distributors and large modern trade retailers in Japan. In Thailand, the company distributes furniture through well-known modern trade retailers, such as Home Pro, Big C, Mega Home, Thai Wasadu, Tesco Lotus, and Global House.

The company, through ECF Power Co., Ltd., has invested in the Minbu project, a 220-MW solar power plant in Myanmar. The project consists of four phases. The first phase with 50 MW already achieved the commercial operating date in September 2019.

KEY OPERATING PERFORMANCE

Table 1: ECF’s Power Project Portfolio as of 30 Mar 2022

Project/Country	Type	Held by ECF (%)	Installed Capacity (MW)	Contracted Capacity (MW)	COD
Myanmar					
Minbu project					
- Phase 1	Solar	20	50	40	Sep 2019
- Phase 2	Solar	20	50	40	Q4 2022
- Phase 3	Solar	20	50	40	2023-2024
- Phase 4	Solar	20	70	50	2023-2024
Total			220	170	

Source: ECF

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS*
Unit: Mil. THB

	Jan-Mar 2022	-----Year Ended 31 December -----			
		2021	2020	2019	2018
Total operating revenues	417	1,585	1,401	1,273	1,442
Earnings before interest and taxes (EBIT)	46	188	172	186	145
Earnings before interest, taxes, depreciation, and amortization (EBITDA)	51	200	192	228	246
Funds from operations (FFO)	14	61	49	98	125
Adjusted interest expense	36	135	133	118	104
Capital expenditures	49	150	100	57	136
Total assets	3,913	3,756	3,545	3,348	3,396
Adjusted debt	2,086	1,996	1,684	1,608	1,299
Adjusted equity	1,337	1,327	1,240	1,242	1,447
Adjusted Ratios					
EBITDA margin (%)	12.3	12.6	13.7	17.9	17.0
Pretax return on permanent capital (%)	5.5 **	5.7	5.5	6.2	5.4
EBITDA interest coverage (times)	1.4	1.5	1.4	1.9	2.4
Debt to EBITDA (times)	10.5 **	10.0	8.8	7.0	5.3
FFO to debt (%)	2.8 **	3.0	2.9	6.1	9.6
Debt to capitalization (%)	60.9	60.1	57.6	56.4	47.3

* Consolidated financial statements

** Annualized with the trailing 12 months

RELATED CRITERIA

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

East Coast Furnitech PLC (ECF)

Company Rating:	BB
Rating Outlook:	Stable

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