EASTERN POWER GROUP PLC

No. 147/2023
9 August 2023

CORPORATES

Company Rating:	BB+
Outlook:	Negative

Last Review Date: 07/12/22

Company Rating History:

Date	Rating	Outlook/Alert
07/12/22	BBB-	Negative
07/12/18	BBB-	Stable
01/12/15	BBB	Stable

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RATIONALE

TRIS Rating downgrades the company rating on Eastern Power Group PLC (EP) to "BB+" from "BBB-". The downgrade comes after the further delays in the commencement operations of EP's wind power projects in Vietnam, which results in weakened cash flow and tightening liquidity. At the same time, we maintain a "negative" outlook due to the lingering uncertainties related to the projects, particularly the commencement date and unsettled tariff.

The rating reflects the expected reliability of EP's earnings to be derived from the wind power projects. The rating also recognizes EP's strong market presence in the printing industry. On the contrary, the rating is weighed down by significant regulatory risks related to EP's investments in Vietnam, the execution risks of the projects, and the dim outlook of the printing industry.

KEY RATING CONSIDERATIONS

Further delays for commercial operations of the wind power projects

The rating downgrade is primarily based on EP's weakened cash flow resulted from the extended delays in the commencements of commercial operations of EP's wind power projects in Vietnam. EP has four wind farms in Vietnam that have long awaited commencing operations, with net capacity of 126 megawatts (MW) when measured in proportion to EP's equity stakes in the projects. Previously, we expected all EP's wind power projects would have a conclusion on the final tariff with Vietnam Electricity (EVN) and commence operation by the second quarter of 2023. As a result of persistent delays, we expect EP to continue attaining low earnings before interest, taxes, depreciation, and amortization (EBITDA) in 2023, derived primarily from a small pool of solar rooftop projects, as well as printing and packaging businesses. The EBITDA interest coverage ratio will likely remain below 1 time while the funds from operations (FFO) will remain in deficit. These suggest weak cash generation and tightening liquidity.

Significant exposure in Vietnam

EP had shaken-up its power portfolio during 2019-2021 by divesting several power projects and utilizing the proceeds from the divestiture to invest in the wind power projects in Vietnam, which currently make up about 95% of the company's total capacity.

As a result, EP's future earnings considerably hinge on the successful materialization of the projects. However, the projects do not proceed as planned due to the impact of the Coronavirus Disease 2019 (COVID-19) pandemic. The projects faced several hindrances, including supply-chain bottlenecks for major components and labor mobility difficulties. Hence, the project timeline and construction costs have deviated from the initial expectation. More importantly, the projects failed to complete construction ahead of the expiry of the feed-in tariff (FiT) in November 2021.

Tariff remains undetermined

EP is highly exposed to respective regulatory risks. Apparently, the company's financial performance has been undermined by the prolonged indecision of the Vietnamese Government on the new FiT, impeding EP's wind power projects to start commercial operations.

In October 2022, the Ministry of Industry and Trade (MOIT) of Vietnam issued a circular, which sets out formulae for EVN to calculate the new FiT for the solar and wind power projects that failed to meet the operational deadlines. In January 2023, MOIT announced the tariff brackets. The ceiling price for onshore wind power projects is VND1,587 per kilowatt-hour (kWh), or about US$6.6 cents per kWh, which is far lower than the original tariff of US$8.5 cents per kWh. EVN and the developers of solar and wind power projects need to negotiate and agree on the tariffs and ensure that they do not exceed the promulgated bracket. However, the tariff brackets are lower than the expectations of project developers, causing delays in price negotiation and wastage of resources. We view the tariff cut and the project cost overrun will have material impacts on the cash generation and return of EP's wind farms.

MOIT has recently employed temporary mobilization of power generation. This scheme would allow all pending renewable projects to commence operations and receive temporary tariff which is 50% of the announced ceiling tariff brackets, provided that they have completed construction and legal requirements. In the meantime, EVN will continue the tariff negotiations.

Expectation of gradual financial recovery

EP has applied for the temporary mobilization scheme. The company expects all wind farms to have a test and commissioning program in the third quarter and commence operations by the end of 2023. In our base case, we assume all projects to commence operation in January 2024 while continuing negotiations for the final tariffs. We assume EP will finalize the tariff negotiation within one year thereafter. Once the official electricity prices are finalized and approved by the authority, we assume the projects will be compensated according to the official price from the date of power supply to the grid. We also assume the final tariff would be equal to the ceiling price, or VND1,587 per kWh. As such, we assume EP will recognize the revenue from the wind farms in full amount, based on the ceiling price. Meanwhile, EP will accrue 50% of revenue as accounts receivable. We assume EP's wind farms to receive the accrued amount in early 2025.

With these assumptions, we forecast EP's revenue to recover to THB1.7-THB1.8 billion per year in 2024-2026. Over the period, we forecast EBITDA to be THB1 billion per year, resulting in the debt to EBITDA ratio declining to 5-6 times. At the same time, we project FFO of THB0.5-THB0.6 billion per year, which could raise the FFO to debt ratio to over 10% in 2025. We expect EP to keep the debt to capitalization ratio in the 45%-55% range. However, we note that EP's net cash flow from operations would stay negative in 2023-2024, before turning to positive from 2025 onwards.

Lingering uncertainties of wind farm projects

We maintain a "negative" outlook as EP's forecast earnings from the wind farms remain susceptible to several uncertainties. Notwithstanding the Vietnamese Government's ongoing efforts to resolve the FiT issues, further delays on the resolution or the commencement of operations remain possible and would pose a serious threat to EP's earnings recovery. Moreover, cash flow from the projects could be curtailed if the final tariff is lower than our base assumption or the payment of accrued revenue is stretched out to a further date.

In addition, wind power generation generally carries significant operational risks, such as mechanical and electrical breakdowns. The success of a wind power project largely hinges on the availability and speed of wind. The performances of EP's wind farms will need to be proven.

Small contribution from printing and packaging businesses

In the printing business, EP's strong market presence is underpinned by its broad range of products, well-established track record, and long-term relationships with its customers. Despite disruptions in the printing and publishing industries, EP's printing business remains profitable. EP has diversified into the paper packaging business in the wake of growing e-commerce and food-delivery demand. In all, gross margin from the printing and packaging business decreased to 9% in 2022 due to higher material costs. However, gross profit margin in the first three months of 2023 recovered to 12% due to the normalized material costs.

In our view, the printing business remains a meager operation while EP's efforts to increase packaging revenue are at slower pace than our expectation. We project the printing and packaging businesses will represent a small slice of EP's earnings over the long term.

Heightened liquidity risk

As of March 2023, the company had cash and cash equivalent of merely THB129 million, while we forecast the company to have deficit cash flow from operations. On the other hand, EP had short-term and long-term debts coming due in the next 12 months, totaling THB1.6 billion. Therefore, EP would likely need to refinance all of its debts. We view EP's tight liquidity could be eased if the company could seek long-term project loans for the wind farms, with repayment schedules matching the project cash flows.

Debt structure

At the end of March 2023, EP had consolidated debt of THB4.7 billion, most of which were unsecured debentures at the company level, with an outstanding amount of THB4.3 billion. The ratio of priority debt to total debt was about 8%. However, the ratio may increase to over 50% if the wind farm project loans materialize.

BASE-CASE ASSUMPTIONS

- Revenue from printing and paper packaging businesses of about THB680-THB800 million per year during 2023-2026, with a gross profit margin of around 12%.
- Solar rooftop projects to produce power yield with a capacity factor of about 8%-16%.
- Energy yield of Vietnam wind farms to reach P90 (the 90% probability level of energy production).
- Revenue from power business to be around THB1 billion per year in 2024-2026.
- EBITDA margin of 17% in 2023, then increasing to above 50% from 2024 onwards.
- Total capital expenditure of THB0.9 billion during 2023-2026.
- EP to obtain project finance loans of THB3.2 billion in 2024 for all its wind power projects in Vietnam.

RATING OUTLOOK

The "negative" outlook reflects the ongoing uncertainties related to EP's wind power projects including the project commencement date, the possible tariff cut, and unclear settlement of accrued electricity charge. We view EP's financial risk will be elevated if the projects face further serious delays in commencing commercial operations, or if cash generation is significantly lower than our base-case forecast.

RATING SENSITIVITIES

We could consider revising the outlook to "stable" if EP's wind power projects start commercial operation as planned. Moreover, the plant performances, the timeline of tariff finalization, and settlement of accrued revenue are in line with our expectations. Given the "negative" outlook, an upward rating revision is unlikely in the near term.

A rating downgrade could emerge as a result of continued weak cash generation. This could occur if EP's wind power projects encounter further delays in the commencement of operations, or they deliver weaker-than-expected cash flow due to low final tariff, underperformance, or delayed settlement of accrued revenue. A rating downgrade could also occur if the company is unable to refinance its debts coming due.

COMPANY OVERVIEW

Formerly named Eastern Printing PLC (EPCO), EP was established in 1990 as a printing service provider. The company was listed on the Stock Exchange of Thailand (SET) in 1993. As of March 2023, Aqua Corporation PLC (AQUA) held approximately 40% of EP while the Chinsupakul Family, the company's founder, owned 23%. EP provides a full range of printing services for both domestic and foreign customers. EP prints newspapers, magazines, product manuals, educational books, calendars, and advertising materials. The company has transitioned to focus heavily on the power business to make up for the drop-off in the printing business. In April 2020, the company changed its name from EPCO to EP. EP's shares were moved from media and publishing sectors to the energy and utility sector on the SET.

EP's power business is carried out by its main subsidiary, Eternity Power PLC (ETP; rated "BB+/Negative"). EP currently owns 81% of ETP. EP launched its two pilot solar farms, with a total capacity of 11 MW, in 2012. The company later expanded with solar power projects in Thailand, Japan, and Vietnam.

The company also invested in two cogeneration power companies, generating and selling electricity under the small power producer (SPP) scheme, through 25-year power purchase agreements (PPAs) with the Electricity Generating Authority of Thailand (EGAT) and long-term contracts with industrial users.

In 2018, EP spent a total of THB490 million to acquire a 100% share of WPS (Thailand) Ltd. (WPS), which helped expand the company's printing facilities. For the power business, EP invested in two solar farms in Vietnam, namely "Xuan Tho 1" and "Xuan Tho 2".

In late 2019, EP sold off the two solar farms in Vietnam after they commenced operation. In 2020, EP sold all operating solar farms from its portfolio. Instead, EP invested in four wind farms in Vietnam, namely "Huong Linh 3" (HL3), "Huong Linh 4" (HL4), "Che Bien Tay Nguyen" (TN), and "Phat Trien Mien Nui" (MN). The four wind farms were initially slated to commence operation by the end of October 2021. EP sold its investments in the cogeneration power plants and small solar farms in Japan in 2021. Currently, EP's power portfolio has an installed capacity of 164.5 MW.

KEY OPERATING PERFORMANCE

Table 1: Total Operating Revenue Breakdown

	2018	2019	2020	2021	2022	Jan-Mar 2022	Jan-Mar 2023
Printing business	42%	37%	34%	54%	45%	51%	42%
Packaging business	1%	1%	7%	34%	32%	38%	39%
Power business	57%	62%	59%	12%	22%	11%	19%
Total	100%	100%	100%	100%	100%	100%	100%
Total revenue (mil. THB)	**979**	**1,530**	**1,145**	**700**	**878**	**197**	**205**

Source: EP

Table 2: Power Project Portfolio (End of Mar 2023)

Project	Plant Type	Held by EP (%)	Installed (MW)	Equity (MWe)	SCOD/ COD
Operating			**7.9**	**6.4**	
Solar rooftop	Solar rooftop	81.4	1.5	1.2	2014-2015
Commercial rooftop	Solar rooftop	81.4	6.4	5.2	2019-2020
Constructing & developing			**156.6**	**126.2**	
HL3	Wind farm	81.4	28.8	23.2	2023
HL4	Wind farm	81.4	28.8	23.2	2023
TN	Wind farm	81.4	49.5	39.9	2023
MN	Wind farm	81.4	49.5	39.9	2023
Total portfolio			**164.5**	**132.6**	

SCOD = Scheduled commercial operation date
COD = Commercial operation date

Source: EP

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS*

Unit: Mil. THB

		-----------Year Ended 31 December ---------			
	Jan-Mar 2023	2022	2021	2020	2019
Total operating revenues	206	894	713	1,168	1,552
Earnings before interest and taxes (EBIT)	(8)	12	139	320	786
Earnings before interest, taxes, depreciation, and amortization (EBITDA)	12	91	(3)	333	659
Funds from operations (FFO)	(64)	(176)	(953)	(35)	217
Adjusted interest expense	67	262	355	282	362
Capital expenditures	33	1,289	4,873	483	821
Total assets	9,692	9,765	11,530	8,382	11,555
Adjusted debt	4,598	4,521	2,520	2,162	6,433
Adjusted equity	4,531	4,616	5,270	4,862	3,897
Adjusted Ratios					
EBITDA margin (%)	5.90	10.18	(0.36)	28.54	42.45
Pretax return on permanent capital (%)	(0.03) **	0.12	1.50	3.33	7.35
EBITDA interest coverage (times)	0.18	0.35	(0.01)	1.18	1.82
Debt to EBITDA (times)	61.35 **	49.65	(982.02)	6.48	9.77
FFO to debt (%)	(4.32) **	(3.89)	(37.84)	(1.63)	3.38
Debt to capitalization (%)	50.36	49.48	32.35	30.78	62.28

* *Consolidated financial statements*
** *Annualized with trailing 12 months*

RELATED CRITERIA

- Group Rating Methodology, 7 September 2022
- Corporate Rating Methodology, 15 July 2022
- Key Financial Ratios and Adjustments for Corporate Issuers, 11 January 2022

Company Rating:	BB+
Rating Outlook:	Negative

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