CreditNews ข่าวเครดิต

RIGHT TUNNELLING PLC

No. 179/2023
21 September 2023

CORPORATES

Company Rating: BB+
Outlook: Stable

Last Review Date: 20/12/22

Rating History:

Date	Rating	Outlook/Alert
20/12/22	BBB-	Negative
01/02/22	BBB-	Stable

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RATIONALE

TRIS Rating downgrades the company rating on Right Tunnelling PLC (RT) to "BB+" from "BBB-" and revises the outlook to "stable" from "negative". The rating downgrade reflects the weaker-than-expected operating performance and material deterioration in RT's financial profile. A smaller equity base from a deeper-than-expected net loss in 2022 and increasing debt loads from lengthy unbilled receivables were the main contributing factors for elevated financial leverage.

The rating continues to reflect RT's modest scale of business, narrow scope of service offerings, and high concentration in a few large construction projects. The rating is also weighed down by the severe competition and cyclicality of the engineering and construction (E&C) industry. Conversely, the rating is supported by RT's well-established track record in tunnel and shaft works and its increasing amount of backlog.

KEY RATING CONSIDERATIONS

Weaker-than-expected operating performance

RT suffered a significant net loss of THB312 million in 2022. The loss was mainly due to the compression of gross margin in several projects amid higher-than-expected construction material costs and slower revenue recognition following delays in several construction projects. Despite significant cost revisions in the last quarter of 2022, these factors have continued to pressure the company's bottom line. In the first six months of 2023 (6M2023), the company reported a further net loss of THB17 million.

Looking ahead, we expect RT's operating performance to improve gradually, supported by increasing backlog, improved margins from more stable raw material prices, and the completion of loss-making projects. Our base-case projects the company's gross margin to bounce back to 12%-13% during 2023-2025. We expect the company to secure new construction contracts worth about THB3-THB4 billion per annum during 2023-2025 in order to maintain its total operating revenue in the range of THB3-THB4 billion per annum. RT's earnings before interest, taxes, depreciation, and amortization (EBITDA) should improve to the range of THB300-THB450 million per annum.

Despite the expected performance recovery, intense competition in the E&C industry and volatile raw material prices remain significant downside risks. Challenging excavation works could also cause unforeseen difficulties, posing risks of project delays and cost overruns. Thus, any further deterioration in RT's operating performance could negatively affect the rating.

Rising financial leverage

RT's financial profile has materially deteriorated over the past three years. Deeper-than-expected net losses caused its equity base to erode to around THB1 billion as of June 2023 from THB1.34 billion as of December 2021. Although we expect the company to return to profit during 2023-2025, it will likely take several years to restore its equity back to the 2021 level. In addition, lengthy collection periods with a continued increase in the sum of outstanding unbilled receivables and accounts receivable have kept working capital requirements high, elevating the company's debt burden and financial expenses. RT's adjusted debt increased to almost THB2 billion as of June 2023, from THB990 million as of December 2021.

Looking ahead, RT's financial leverage will depend largely on its capability to bring down the outstanding unbilled receivables and accounts receivable. The company's outstanding debt could drop significantly once it receives payments from the project owners, however, the timeframe remains uncertain. Under TRIS Rating's base case, we project RT's cash conversion cycle to gradually decline from its peak of 192 days in 2022 to approximately 100-120 days in 2025. Therefore, its net debt to EBITDA ratio should improve to around 4-6 times over the next 2-3 years. Its debt to capitalization ratio is expected to range from 55%-65%, higher than our previous target of 47%-54%.

Modest business scale with high concentration on large projects

RT's business scale, as measured by revenue and asset base, is considered modest compared with its rated peers. Also, its operating performance has been dominated by a few large projects. Revenue from the five largest remaining projects made up almost half of total revenue in 6M2023. The five largest projects under construction accounted for nearly 80% of its backlog as of June 2023. Failure to complete one large project or any significant disruption to a project could result in a material impact on its financial results.

However, looking forward, the company will likely benefit from the government's efforts to improve the country's infrastructure. We expect several potential projects to involve excavation works in which the company has expertise. RT secured new construction contracts worth THB6.7 billion in 2022 and THB2.7 billion in 6M2023, including the Double-Track Denchai-Chiang Rai-Chiang Khong railway and the Luang Prabang hydropower project, worth THB5.9 billion in total, boosting its backlog to more than THB10 billion as of June 2023. The increasing backlog should enhance its revenue base from THB2-THB3 billion per annum to THB3-THB4 billion per annum during 2023-2025.

Well-established track record in tunnel and shaft works

TRIS Rating expects RT to maintain its competitive edge in tunnel and shaft works. In our view, RT's strength is supported by its experienced management team, engineers, and geologists, as well as a wealth of machinery and equipment. The company focuses on tunnel and shaft works, dam construction, hydro power plants, pipe jacking, and horizontal directional drilling, mostly for public sector clients.

RT has been involved in several large-scale projects, including tunnelling the diversion and power waterways of Nam Ngum 2 hydropower plant and major civil works for the powerhouse of the Xayaburi hydropower plant. Both are part of the large-scale hydropower plants in the Lao People's Democratic Republic (Lao PDR). The company is also working on the tunnelling works of the Dual-Track Rail Route Project for the Northeastern Line (Map Kabao-Thanon Chira Junction), the Mae Taeng-Mae Ngat Project, and the Sri Song Rak Floodgate Project. These three projects should strengthen its track record, increasing its chances of successfully bidding for future construction contracts.

Manageable liquidity

RT's liquidity should remain manageable in the year ahead. As of June 2023, the company had debts due over the next 12 months of THB870 million, comprising short-term loans, mainly promissory notes (P/N), worth THB576 billion, long-term loans of THB157 million, and lease liabilities of THB137.0 billion. The repayment of short-term loans is rather flexible as the banks normally extend or rollover the loan tenor to match the project timeline. The repayment of short-term loans will come from the proceeds received from project owners. The maturing long-term loans should be covered by its funds from operations (FFO). Moreover, the company had cash on hand of THB205 million, undrawn credit facilities of around THB115 million, and expected FFO of THB187 million to further support its liquidity and future construction works.

A key financial covenant on RT's debentures requires maintenance of an interest-bearing debt to equity ratio below 2.5 times. As of June 2023, the ratio was about 2.46 times. We expect the company to carefully manage its capital structure to avoid a covenant breach. The covenant on its bank loans requires RT to maintain a debt service coverage ratio covenant on its bank loans of above 1.1 times. The ratio was -0.21 times in 6M2023, well below the required level. However, given the company's record of delivering construction projects as planned and the earnings recovery prospect, we expect RT to receive covenant waivers from its lenders.

Debt structure

At the end of June 2023, RT's total debt, as per our priority debt calculation, was approximately THB2.1 billion. RT's priority debt, including secured debts at the company and total debt at the subsidiaries, was about THB0.85 billion. This translates to a priority debt to total debt ratio of 40%.

BASE-CASE ASSUMPTIONS

- RT to secure new construction contracts worth about THB3-THB4 billion per year during 2023-2025.
- Total operating revenue of THB3-THB4 billion per year during 2023-2025.
- EBITDA margin in the 9%-12% range during 2023-2025.
- Total capital spending of around THB250 million per year during 2023-2025.

RATING OUTLOOK

The "stable" outlook reflects our expectation that RT will maintain its competitive edge in tunnel and shaft works and secure new projects as targeted. Furthermore, we expect the company's operating performance and financial leverage to remain in line with our projections.

RATING SENSITIVITIES

A credit upside on RT would materialize if RT's financial performance significantly improves such that its EBITDA stays around THB500 million and its net debt to EBITDA ratio stays below 4 times on a sustained basis. On the contrary, the rating and/or outlook could be revised downward should its operating performance and/or financial profile turn out to be worse than our expectations. This could be due to project delays, cost overruns, or inefficient working capital management, such that the net debt to EBITDA ratio stays above 7 times for an extended period.

COMPANY OVERVIEW

RT was founded in 2000 by Mr. Chawalit Tanomtin and listed on the Stock Exchange of Thailand (SET) in 2020. Mr. Chawalit Tanomtin, the founder, remains the major shareholder, holding approximately 16% of the company's shares as of June 2023. The company is a contractor specializing in geotechnical works, covering tunnel and shaft construction, dam construction, hydro power plants, pipe jacking, and horizontal directional drilling. RT is also engaged in slope protection and stabilization work, earth and rock excavation, and geological exploratory drilling services. Revenue from tunnel and shaft construction remains the key source of revenue, accounting for 46% of total revenue during the first six months of 2023, followed by dam construction and irrigation systems which contributed 21% of total revenue.

KEY OPERATING PERFORMANCE

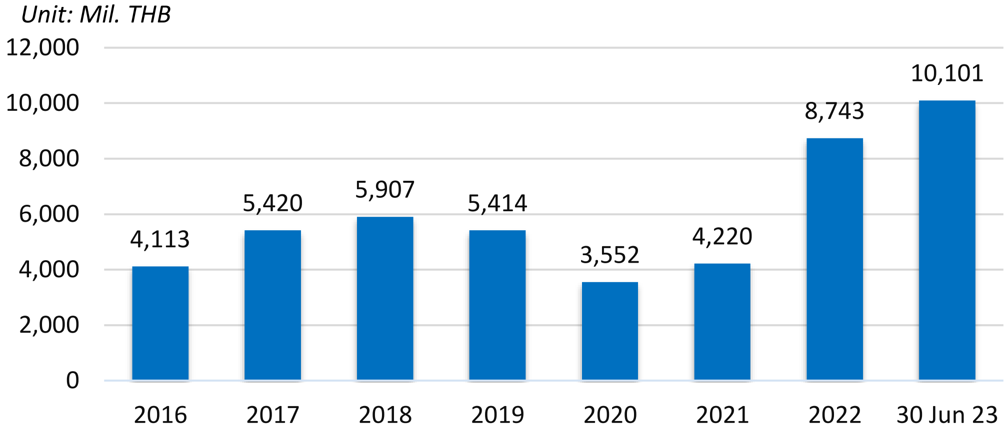
Table 1: Revenue Breakdown by Type of Project

Unit: %

Type of Project	2017	2018	2019	2020	2021	2022	Jan-Jun 2023
Tunnel & Shaft Construction	33	65	61	59	51	32	46
Dam Construction & Irrigation System	7	1	2	8	20	33	21
Hydropower Plant	41	16	4	1	-	-	2
Pipe Jacking & Horizontal Directional Drilling	13	11	11	12	15	15	8
Others	6	7	22	20	13	20	23
Total	**100**	**100**	**100**	**100**	**100**	**100**	**100**

Source: RT

Chart 1: Backlog



Source: RT

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS*

Unit: Mil. THB

	Jan-Jun 2023	-------------Year Ended 31 December -------- 2022	2021	2020	2019
Total operating revenues	1,457	2,053	2,488	2,860	2,351
Earnings before interest and taxes (EBIT)	50	(302)	100	364	230
Earnings before interest, taxes, depreciation, and amortization (EBITDA)	140	(146)	255	550	500
Funds from operations (FFO)	62	(227)	198	428	382
Adjusted interest expense	70	77	54	68	75
Capital expenditures	53	84	32	28	135
Total assets	5,508	4,515	3,915	4,050	3,731
Adjusted debt	1,942	1,527	990	525	1,155
Adjusted equity	1,013	1,030	1,337	1,389	587
Adjusted Ratios					
EBITDA margin (%)	9.62	(7.09)	10.25	19.24	21.26
Pretax return on permanent capital (%)	(7.71) **	(10.69)	3.83	15.66	12.67
EBITDA interest coverage (times)	2.01	(1.89)	4.72	8.09	6.68
Debt to EBITDA (times)	(25.24) **	(10.49)	3.88	0.95	2.31
FFO to debt (%)	(10.47) **	(14.90)	19.99	81.52	33.04
Debt to capitalization (%)	65.72	59.72	42.55	27.44	66.29

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

RELATED CRITERIA

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

Right Tunnelling PLC (RT)

Company Rating:	BB+
Rating Outlook:	Stable

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