TRIS RATING
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SPCG PLC

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CORPORATES

Company Rating:	A-
Issue Ratings:	
Senior unsecured	A-
Outlook:	Stable

Last Review Date: 18/06/20

Company Rating History:

Date	Rating	Outlook/Alert
17/08/17	A	Stable
04/06/15	A-	Stable
02/05/14	BBB+	Stable

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RATIONALE

TRIS Rating downgrades the company rating on SPCG PLC (SPCG) and the ratings on its outstanding debentures to "A-" from "A", with a "stable" rating outlook. At the same time, TRIS Rating assigns a rating of "A-" to SPCG's proposed issue of up to THB5 billion in senior unsecured debentures. The company intends to use the proceeds from the proposed debentures to fund the new solar farm project.

The downward revision of ratings reflects the imminent contraction in earnings generated by its core power assets due to the gradual phase-out of additional tariff (adder). It also mirrors the expected surge in SPCG's debt loads to support the sizable investment in solar farm projects in the new city of Eastern Economic Corridor Special Development Zone (EEC). The ratings continue to reflect reliable cash flow from solar power plants. However, the ratings are constrained by the increasingly challenging business environment of the solar power industry.

KEY RATING CONSIDERATIONS

Reliable cash flow from solar power

SPCG has reaped robust revenues and earnings from its core power assets, comprising 36 operating solar farms in Thailand. The cash flow from solar power generation is largely predicable thanks to low operational risks and high creditability of the power purchaser. SPCG's existing power plants operate under long-term Power Purchase Agreements (PPAs) signed with the Provincial Electricity Authority (PEA) on a non-firm basis. With a total contracted capacity of 205.92 megawatts (MW) under the PPAs, all solar farms have benefited from the adder of THB8 per kilowatt-hour (kWh) on top of the base tariff for 10 years after the commercial operation date (COD).

On average, SPCG's solar farms have rendered satisfactory performance. The annual output of most solar power plants consistently outperforms the P50 level (the 50% probability of energy production), the threshold of expected operating performance. Accordingly, SPCG's portfolio generated power of 385-397 gigawatt-hour (GWh) per year during 2018-2020.

Earnings from existing solar farms on declining stage

The downgrade of ratings reflects the imminent contraction of earnings generated from its core solar farms. We expect to see a material decline in earnings from 2021 onwards when a number of solar power assets will no longer benefit from the adder. Towards the end of 2023, there will be 23 solar farms (or 63% of total contracted capacity) receiving only the base tariff for power sales. Given the phase-out of adder, we estimate the average tariff will tumble from THB11 per kWh in 2020 to THB7 per kWh in 2023. In our base-case forecast, earnings before interest, tax, depreciation, and amortization (EBITDA) from the core power assets will decline by about THB0.5-THB1 billion per year during 2021-2023.

Looking further ahead, earnings from SPCG's core solar farms will drop sharply in 2024 and 2025 when all adders expire entirely. We estimate the average tariff to decline to around THB3 kWh by that time.

Challenging business environment

SPCG is under acute pressure to restore its earnings after the adder expiration. SPCG has endeavored to sell electricity to industrial users under private PPAs but the capacity is relatively small, given the intense competition.

We view it is inevitable for SPCG to adjust its business strategy, to adapt to the increasingly changing business environment for solar power business. The investment opportunities for solar power in Thailand appear to be significantly losing their appeal, due to the cut-off of incentive tariff, highly competitive market, repeated delays in public projects, and lower return on investment. Solar power producers have moved towards offering electricity to industrial users under private PPAs, which entails higher counterparty risk than public projects. Given the dearth of new opportunities, acquisitions and divestiture of existing power projects have become the trend.

Seeking opportunities outside Thailand, SPCG has invested in Ukujima Solar Project, a 480-MW solar farm located in Ukujima island, Japan. In total, SPCG will spend THB2.7 billion for 17.9% shares in the project. Given a multi-year period of project construction, the project is expected to commence operation in 2023. We expect SPCG will earn around THB500 million in dividend a year from this investment from 2024 onwards.

New solar power project in EEC

SPCG expects to secure future earnings with the 500-MW solar farms project in the new city of EEC. SPCG holds 80% interest in the project company, SET Energy Co., Ltd. (SET Energy), whereas PEA ENCOM International Co., Ltd. (PEA-ENCOM) holds 20%. This much-anticipated project is set to serve potential electricity demand in EEC, with total project cost of approximately THB23 billion. SET Energy will sell electricity to PEA via PEA-ENCOM under 25-year PPAs. The volume of electricity sales to PEA shall not exceed the monthly consumption in the new city area and the five sub-districts in Bang Lamung district. The tariff is based on the wholesale tariff that the Electricity Generating Authority (EGAT) sells to PEA according to the actual connected voltage level.

Of total 500 MW, SPCG is aiming to launch the initial phase of 315 MW in 2021, which will cost about THB15 billion. In our base-case forecast, we assume the project construction will start in 2021. The initial phase will comprise 22 solar farms and start commercial operations from second and fourth quarter of 2022. We estimate the project will bring in THB630 million in revenue in 2022 and generate approximate THB1.2 billion each year thereafter. We view that the project will render predictable cash flow, propelled by low operation risk and credible power buyer. However, we consider the project is exposed to a range of downside risks, including (i) lower-than-expected electricity demand in the area, (ii) the actual tariff rate which could be lower than our base-case assumption, and (iii) the delay of projects caused by relevant regulatory requirements.

Expected surge in debt load

According to our base-case forecast, earnings from new solar projects in EEC will not be enough to offset the drop in revenue from the adder expirations. We project SPCG's EBITDA to total THB3.2 billion in 2021, or a 20% drop from THB4.0 billion in 2020. EBITDA will decline further to THB3.1 billion in 2023. We forecast EBITDA margin (EBITDA as a percentage of revenue) will decline to 66% in 2023, in contrast to 82% in 2020.

We estimate the new project's initial phase will cost about THB15 billion, which is relatively high compared with SPCG's asset size. SPCG plans to fund the new solar project primarily by debt. The company will use the proceeds from THB5 billion senior unsecured debentures for the capital injection to SET Energy. At the same time, SET Energy will seek financing from financial institutions to fund 75% of project cost. On a consolidated basis, we forecast SPCG's debt to soar to nearly THB14 billion in 2022-2023, a sharp increase from THB2.1 billion in 2020. As a result, we forecast the ratio of debt to EBITDA to surge to 4.5 times in 2023, a hefty increase from 0.5 times in 2020. The ratio of debt to capitalization will rise to 41% in 2023, compared with 11% in 2020. These suggest a heightened financial risk.

We note that the ratings on debentures issued SPCG, the parent, could be lowered to be one notch below the company rating in the future due to the potential structural subordination. As the debt at SET Energy, the operating subsidiary, is set to increase over the course of project development, we expect it will increase the level of priority debt at the parent level with the potential of triggering a downward revision on the issue ratings due to structural subordination.

We assess SPCG having ample liquidity over the next 12 months. As of December 2020, SPCG had cash and cash equivalent of approximately THB2.5 billion which is enough for the redemption of debentures coming due throughout the year 2021.

BASE-CASE ASSUMPTIONS

- New solar projects in EEC area to be constructed in 2021 and start operation during second and fourth quarter of 2022
- During 2021-2023, annual power output to be in the range of 357-764 GWh.
- Total revenues are projected to be THB4.6-THB4.9 billion during 2021-2023, while EBITDA margin is forecast at 70% in 2021 and drop to 66% in 2023.

- Total capital expenditures of around THB15 billion during 2021-2023 and total investment in solar projects in Japan of THB1.4 billion over the same period.
- New issue bonds of THB5 billion in 2021
- Bond repayments of THB2.2 billion in 2021, THB1.3 billion in 2022, and THB0.65 billion in 2023.
- Dividend pay-out of THB1.3 billion per year during 2021-2023.

RATING OUTLOOK

The "stable" outlook reflects our expectation that SPCG's existing portfolio will be capable of maintaining its plant performance ratio at a satisfactory level above 75% over the next three years, and that the new solar farms in EEC will be developed and generate cash flow as planned, with SPCG's operating performance and financial leverage to be in line with our forecast range.

RATING SENSITIVITIES

The prospect of a rating upgrade is limited, given the negative impact from the imminent phase-out of adder. In addition, SPCG's financial profile is set to weaken due to the debt-financed investment in the solar farm project in EEC.

On the contrary, a downward revision to the ratings could emerge if SPCG's cash flow weakens considerably, which might occur if the plant performance significantly falls short of our forecast or SPCG's efforts to counteract the weakening cash flow do not yield the expected results. A negative rating pressure could also arise if SPCG's financial risk is further heightened due to excessive use of debt to fund new investments.

COMPANY OVERVIEW

SPCG was founded in 1996 as Solar Power Co., Ltd. (SPC) to develop solar power projects in Thailand. In 2011, the company was listed on the Market for Alternative Investment (MAI), through a reverse listing process, and renamed SPCG. In 2012, SPCG moved its listing to the Stock Exchange of Thailand (SET). As of March 2020, the Khunchornyakong family held a 37% interest in SPCG. SPCG is a holding company, investing in 36 solar farms with a total installed capacity of 260.35 MW.

SPCG's strong business profile is buoyed by the reliable cash flows it earns from investing in solar power projects. SPCG, through its operating subsidiaries, owns 36 operational solar power plants. All of the plants have PPAs with PEA and will receive a tariff adder of Bt8 per kWh on top of the normal tariff for 10 years. The company's solar farms are located in nine provinces in the Northeastern region of Thailand and in Lopburi province. The Northeastern region is best suited for solar power production, based on the statistics for solar irradiation levels in the area.

SPCG has strived to seek new project investments to replenish its dwindling earnings. The company has recently invested in Ukujima Solar Project, a 480-MW solar farm located in Ukujima island, Japan. In total, SPCG will spend THB2.7 billion for 17.9% shares in the project, along with reputable partners, such as, Kyudenko Corporation, Kyocera Corporation. Given a multi-year period of project construction, the project is expected to commence operation in 2023. We expect SPCG will earn around THB500 million in dividend a year from 2024 onwards.

Recently, the company is bent on developing the solar farm project in EEC area. SPCG holds 80% shares in the project through its subsidiary, SET Energy. PEA-ENCOM, a subsidiary of PEA, holds the rest of 20%. The project will produce and distribute the electricity to PEA under the electricity charged rate sold to EGAT to PEA and deduct THB1 satang per each kWh. In November 2020, SET Energy entered into a power purchase agreement with PEA ENCOM. The PPA has term of 25 years with option to extend for 5 years in each time.

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS

Unit: Mil. THB

	---------------------- Year Ended 31 December -------------------				
	2020	**2019**	**2018**	**2017**	**2016**
Total operating revenues	4,941	5,260	5,997	6,015	5,460
Earnings before interest and taxes (EBIT)	3,374	3,365	3,479	3,437	3,301
Earnings before interest, taxes, depreciation, and amortization (EBITDA)	4,053	4,036	4,170	4,081	3,954
Funds from operations (FFO)	3,704	3,639	3,605	3,398	3,199
Adjusted interest expense	266	361	504	618	746
Capital expenditures	38	31	17	90	91
Total assets	21,718	21,903	22,798	23,027	24,232
Adjusted debt	2,134	3,417	6,776	9,220	10,700
Adjusted equity	17,156	15,604	13,881	11,208	9,766
Adjusted Ratios					
EBITDA margin (%)	82.03	76.73	69.54	67.85	72.42
Pretax return on permanent capital (%)	15.76	15.42	15.80	15.29	13.93
EBITDA interest coverage (times)	15.23	11.19	8.28	6.60	5.30
Debt to EBITDA (times)	0.53	0.85	1.62	2.26	2.71
FFO to debt (%)	173.59	106.50	53.21	36.86	29.89
Debt to capitalization (%)	11.06	17.96	32.80	45.13	52.28

RELATED CRITERIA

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

SPCG PLC (SPCG)

Company Rating:	A-
Issue Ratings:	
SPCG21DA: THB1,700 million senior unsecured debentures due 2021	A-
SPCG22DA: THB1,250 million senior unsecured debentures due 2022	A-
SPCG23DA: THB650 million senior unsecured debentures due 2023	A-
Up to THB5,000 million senior unsecured debentures due within 10 years	A-
Rating Outlook:	Stable

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