TTCL PLC

No. 2/2016 7 January 2016

Company Rating: BBB+

Issue Ratings:
Senior unsecured BBB+

Outlook: Stable

Company Rating History:

Date	Rating	Outlook/Alert
28/03/14	BBB+	Stable

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Rating Rationale

TRIS Rating affirms the company and senior unsecured debenture ratings of TTCL PLC (TTCL) at "BBB+". The ratings reflect TTCL's strong market position in the domestic EPC (engineering, procurement, and construction) sector, its capability of undertaking larger projects in Thailand and abroad, as well as its strategic diversification to the power business. However, these strengths are partially offset by the heightened leverage, the operating risks of EPC projects abroad, the cyclicality of the EPC business, and severe competition.

TTCL is an EPC contractor based in Thailand. TTCL was established in 1985 as a joint venture between Italian-Thai Development PLC (ITD) and Toyo Engineering Corporation (TEC), a Japanese EPC firm. TTCL went public in 2008 and was listed on the Stock Exchange of Thailand (SET) a year after. As of 18 December 2015, TEC held approximately 17.4% of the company's shares outstanding, while Chiyoda Corporation, based in Japan, owned 3%, and ITD owned 3.3%. Positioned as an integrated EPC contractor, TTCL primarily constructs industrial plants including petrochemical and refinery, chemical, fertilizer, oil and gas, and power plants. In 2010, TTCL expanded into the power business, a move aimed at investing in propitious power projects, which helps reduce its susceptibility to cyclicality and the stiff competition in the EPC business.

The ratings reflect TTCL's strong position in the domestic EPC market, particularly in the industrial plant segment. The company is among the top-tier SET-listed contractors, considering revenue base and asset size. The company's good reputation for project execution and quality performance is underscored by a list of well-respected and creditworthy customers, including large refining and petrochemical companies. A proven track record, together with know-how and experience, should help the company retain its market position over the medium term.

The ratings also recognize TTCL's ability to undertake large EPC projects and expand geographically. Notwithstanding the concentration risk stemming from large projects, TTCL has increased its sizable backlog during the past several years. A large backlog secures future revenues. As of September 2015, TTCL's backlog soared to Bt34.7 billion. The total value of the current projects in the backlog will be realized 20% of TTCL's revenues during 2015, 75% in 2016, and 45% in 2017, according to TRIS Rating's base-case forecast. TTCL, along with its subsidiaries and branches abroad, has undertaken EPC projects in neighbouring countries, as well as Qatar, the Philippines, and the United States (US). Geographical diversification supports the ratings. TTCL achieved record revenue of nearly Bt20 billion in 2014, half of which were recognized from projects abroad.

The ratings also take into account TTCL's business strategy to expand its scope of business to power producer. TTCL has invested in power projects so it will have steady sources of income from multi-year power purchase agreements. Moreover, TTCL engaged in EPC work for all the power projects and received EPC income as well. The company has invested in natural gas-fired, biogas, and solar power plants. TTCL commenced its power business in 2010 when it invested in 42% of the preferred shares of Nava Nakorn Electricity Co., Ltd. (NNE). NNE operates a 110-megawatt (MW) combined cycle gas turbine power plant. The company also invested and built a 120-MW gas-fired power plant in Ahlone, Myanmar; the "Ahlone Project". TTCL, through its Myanmar-based subsidiary, owns around 72%

of the Ahlone project, which carries a total investment cost of Bt5,500 million. TTCL is making good progress with its diversification strategy. The power segment has generated a sizable amount of EBITDA (earnings before interest, taxes, depreciation, and amortization) as the Ahlone power plant is starting to pay off. For the first nine months of 2015, the power segment accounted for around 60% of TTCL's EBITDA, or Bt311 million. Looking ahead, the power business should earn fruitful returns and help sustain TTCL's profitability.

Conversely, the ratings are constrained by TTCL's weakened capital structure. A debt-funded expansion weakened TTCL's capital structure. TTCL borrowed more to fund its working capital needs and the extensive investments for the power projects, particularly in the project in Myanmar. The company plans to invest and build a 1,280-MW coal-fired power plant in Myanmar. This project will cost Bt100,000-Bt103,000 million, which will push up TTCL's leverage.

The ratings are also partly offset by the operating risks associated with projects abroad, despite the benefits TTCL receives from geographical diversification. In addition, the ratings are tempered by cyclicality of the EPC segment, which stands to suppress revenue and profits. Moreover, severe competition among contractors will slash TTCL's profit margins.

TTCL's financial profile for the first nine months of 2015 was lower than TRIS Rating's base-case scenario. The leverage level was higher than expectation due largely to the working capital needs for the large-scale projects. The operating margin (operating profit before depreciation and amortization as a percentage of revenue) was 2.38% in 2014 and 3.04% in the first nine months of 2015, decreasing from an average of 5.5% during 2011-2013. TRIS Rating's base-case scenario, excluding the investment in the 1,280-MW coal-fired power plant project, expects that TTCL's revenue will be at least Bt19,000-Bt24,000 million per annum during 2015-2018. The operating margin is expected to improve gradually to 5%-6% during 2015-2018. Operating income is expected to rise because the company will receive income from the Ahlone project. Funds from operations (FFO) are expected at Bt600-Bt700 million per annum.

During 2015-2018, TRIS Rating's base-case scenario expects TTCL's net debt to equity ratio will stay below 1.2 times. Cash flow protection, as measured by the FFO to total debt ratio and the EBITDA interest coverage ratio, is expected to improve. TTCL will receive more income from its investment in the Ahlone project, pushing the cash flow protection measures higher. The planned investment in the 1,280-MW coal-fired power plant could materially change TTCL's capital structure. During 2015-2018, the FFO to total debt ratio is expected to average around 7%, while the EBITDA interest coverage ratio will hold at 3 times or more.

Rating Outlook

The "stable" outlook reflects the expectation that TTCL will maintain its strong market position in the domestic EPC sector. The operating margin is expected to stay between 5%-6% and the total debt to capitalization ratio will stay below 55%, or debt to equity lower than 1.2 times during 2015-2018.

The uplifted ratings are unlikely to occur in the near term but could emerge if TTCL's operating performance is better than expected and its leverage falls significantly. However, the upside may be outweighed by TTCL's planned investments in large projects, which is likely to put pressure on its financial profile. There is also some credit downside if TTCL's profitability deteriorates further or the total debt to capitalization ratio rises above 60% for a sustained period. Should TTCL make any large-scale investments, the ratings will take into consideration the execution risk, the quality of the projects, and the funding structure.

TTCL PLC (TTCL)

Company Rating:	BBB+
Issue Rating:	
TTCL175A: Bt1,000 million senior unsecured debentures due 2017	BBB+
Rating Outlook:	Stable

KEY RATING CONSIDERATIONS

Strengths/Opportunities

- Strong market position in domestic EPC sector
- Capability of undertaking larger projects in Thailand and abroad
- Moderate backlog size
- Strategic diversification to the power business

Weaknesses/Threats

- Cyclical nature of the EPC sector
- Operating risks of EPC projects abroad
- Heightened leverage

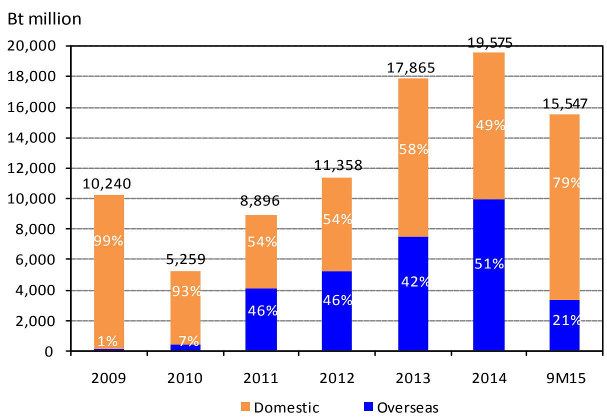
CORPORATE OVERVIEW

TTCL is an EPC contractor based in Thailand. The company provides EPC services for turnkey construction projects. TTCL was incorporated in 1985 as a 51:49 joint venture between ITD, the largest contractor in Thailand, and TEC, an EPC contractor in Japan. TTCL went public in 2008 and was listed on the SET in 2009. In 2010, Chiyoda Corporation, the second-largest EPC contractor in Japan, became TTCL's second-largest shareholder by acquiring 7% of TTCL. As of December 2015, TEC and Chiyoda Corporation sold some of their shares of TTCL. TEC diluted its stake to 17.4% of shares outstanding, from 22.3%. Chiyoda Corporation reduced its shareholding from 7% to 3%. ITD owned 3.3%.

Positioned as an integrated EPC contractor, TTCL primarily constructs industrial plants including petro-chemical and refinery, chemical, fertilizer, oil and gas, and power plants. In 2010, TTCL expanded into the power business, a move aimed at investing in propitious power projects, which helps reduce its susceptibility to cyclicality and the stiff competition in the EPC business.

TTCL achieved revenue of nearly Bt20 billion in 2014, half of which was recognized from projects abroad. For the first nine months of 2015, revenue was Bt15.5 billion. Revenue from domestic projects accounted for about four-fifths of total revenue.

Chart 1: TTCL's Revenue Contribution Breakdown



Source: TTCL

BUSINESS ANALYSIS

- ***Strong market position in domestic EPC sector***

TTCL's ratings reflect its strong position in the domestic EPC market, particularly in the industrial plant segment. The company is one of the top SET-listed contractors, judging from revenue base and asset size. TTCL's market position is protected by certain barriers to entry, such as technical know-how and a proven track record. The company's good reputation of execution projects and the quality of its performance is underscored by a list of well-respected and creditworthy customers, including large refining and petrochemical companies. The strong credit profiles of its customers help lower TTCL's counterparty risks. A proven track record, together with know-how and experience, should help the company retain its market position over the medium term.

- ***Capability of undertaking larger projects in Thailand and abroad***

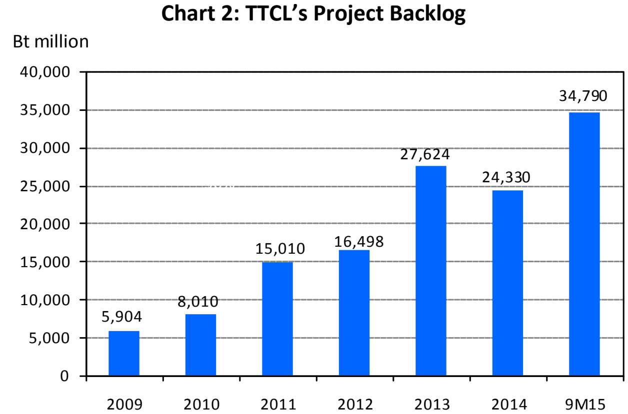
The ratings recognize TTCL's ability to undertake large EPC projects and expand geographically. Notwithstanding the concentration risk stemming from large projects, TTCL has increased its sizable backlog during the past several years. TTCL, along with its subsidiaries and branches abroad, has undertaken EPC projects in neighbouring countries, as well as Qatar, the Philippines, and the US. Geographical diversification supports the ratings.

TTCL has expanded its scope to projects abroad since 2011. The company was able to win bidding at a project sized between US$100-US$200 million during 2011-2013. TTCL is making the transition to a mid-tier international EPC contractor, supported by a proven track record. Currently, the company can undertake EPC projects sized between US$200-US$500 million without the need of any financial or technical support from its founding shareholder, TEC.

- ***Moderate backlog***

TTCL has increased its sizable backlog during the past several years. The backlog increased from Bt8 billion in 2010 to Bt24 billion in 2014. A large backlog secures future revenues.

Chart 2: TTCL's Project Backlog



Source: TTCL

As of September 2015, TTCL's backlog soared to Bt34.7 billion. The total value of the projects in the backlog will be converted to revenue over the next two years. Projects in the backlog will comprise 20% of TTCL's revenues during 2015, 75% in 2016, and 45% in 2017, according to TRIS Rating's base-case forecast. Domestic projects make up 36% of the backlog, while projects abroad make up 54%. TTCL's backlog of projects abroad is mainly from projects in three countries: Malaysia, Vietnam, and Qatar. Projects in these three countries account for 70% of the total backlog of projects abroad. TRIS Rating's base-case scenario expects TTCL will secure new contracts worth around Bt20-Bt25 billion per annum during 2015-2018.

- ***Strategic diversification to the power business***

TTCL has a strategy to expand its scope of business to become a producer of electrical power. TTCL has invested in power projects so it will have steady sources of income from multi-year power purchase agreements. Moreover, the company performed the EPC work for all the power projects and received income as the EPC contractor as well. The company has invested in natural gas-fired, biogas, and solar power plants.

The diversification into power started in 2010 when TTCL bought 42% of the preferred shares of NNE. NNE operates a 110-MW combined cycle gas turbine power plant. TTCL owns 25% of an 8-MW solar farm in Angthong province. The company invested in and built a 120-MW gas-fired power plant in Ahlone, Myanmar. This project is called the "Ahlone project". TTCL, through its Myanmar-based subsidiary, owns around 72% of the Ahlone project, which carries a total investment cost of Bt5,500 million. TTCL is making good progress with its diversification strategy. The power segment has generated a sizable amount of EBITDA as the Ahlone power plant is starting to pay off. For the first nine months of 2015, the power segment accounted for around 60% of TTCL's EBITDA, or Bt311 million. Looking ahead, the power segment should post fruitful returns and help sustain TTCL's profitability.

Going forward, TTCL plans to invest and build a 1,280-MW coal-fired power plant in Myanmar. This new project will cost Bt100,000-Bt103,000 million.

- ***Operating risks of EPC projects abroad***

TTCL's international expansion efforts, especially its investments in Myanmar, carry country risk and have higher administrative costs during the early stages of the projects. Notwithstanding its economic potential, Myanmar remains one of the world's least developed states and lacks sufficient infrastructure, energy, and skilled labor. The country's political risks and stability risks remain substantial, despite a smooth general election held last November. Myanmar-based investments are unavoidably exposed to the substantial risks, such as country, regulatory, and operational risks. As the political transition takes place in early 2016, the policies of the new government towards foreign direct investment remain somewhat uncertain, though the new administration is expected to welcome foreign direct investment. TRIS Rating is of the opinion that Myanmar will take years to become a stable investment climate. The investments in Myanmar thus remain rating concerns. Apart from Myanmar, TTCL has undertaken EPC work in several other countries.

The ratings are partly offset by the operating risks associated with projects abroad, despite the benefits TTCL receives from geographical diversification. In addition, the ratings are tempered by cyclicality of the EPC segment, which adds variability to revenues and profits. Moreover, severe competition among international contractors may slash TTCL's profit margins.

FINANCIAL ANALYSIS

- ***Revenues are expected to stay above Bt20 billion per annum***

TTCL generated revenues of Bt15.5 billion in the first nine months of 2015. Revenues from domestic projects accounted for more than 75% of its total revenues. Based on its backlog of Bt34.7 billion at the end of September 2015, and the new contracts worth at least Bt20 billion per annum that TTCL expects to sign each year, revenue in the EPC segment is expected to be in the range of Bt19-Bt24 billion per annum. Since the company's backlog secures 75% of its revenues during 2016 and 45% in 2017, the downside risk is moderate. In addition, TTCL is expected to have more recurring income from its investment in the Ahlone project. The revenue contributions from its investments are expected to be Bt750-Bt850 million per annum, starting in 2015.

- ***Operating margin is expected to improve***

TTCL's operating margin was 2.38% in 2014 and 3.04% in the first nine months of 2015, decreasing from an average of 5.5% during 2011-2013. The operating margin decreased due to cost overruns in a desalination phase 1 project in Qatar and a refinery and petrochemicals project in Malaysia. A desalination phase 1 project was completed in 2015, while the project in Malaysia, worth Bt10.9 billion, is in the backlog and will be completed in 2018.

During 2015-2018, TTCL's operating margin is expected to improve gradually to 5%-6% due to the larger contributions from the high-margin power segment, especially from the Ahlone project.

- ***Higher leverage will pressure the financial profile***

TTCL had been debt-free for the past several years. Since 2013, TTCL's debt level accelerated as the company invested in power plant projects. TTCL's financial profile for the first nine months of 2015 was lower than TRIS Rating's base-case scenario. As of September 2015, the total debt to capitalization ratio was 56.1%, up from 53.5% in 2014. The leverage level was higher than expected due largely to the working capital needs for the large-scale projects.

The ratings are constrained by TTCL's weakened capital structure, caused by a debt-funded expansion. TTCL borrowed more to fund its working capital needs and fund the extensive investments in the power projects, particularly in the project in Myanmar. In addition, the planned investment in the 1,280-MW coal-fired power plant could materially change TTCL's capital structure.

During 2015-2018, TRIS Rating's base-case scenario, excluding the investment in the 1,280-MW coal-fired power plant project, forecasts TTCL's net debt to equity ratio will stay below 1.2 times. TTCL is expected to keep its debt to capitalization ratio below 55% in order to maintain its ratings at these levels.

- ***Acceptable liquidity profile***

Due to the expected rise in the debt level, TTCL's financial flexibility is expected to weaken in the medium term. However, TTCL's liquidity profile is acceptable. As of September 2015, it had Bt1,145 million in cash on hand. TTCL uses short-term debt and unsecured debentures to fund its working capital needs for the large-scale projects.

TRIS Rating's base-case scenario expects TTCL's FFO will be Bt600-Bt700 million per annum. Cash flow protection, as measured by the FFO to total debt ratio and the EBITDA interest coverage ratio, is expected to improve. TTCL will receive more income from its investment in the Ahlone project, which will push the cash flow protection measures higher. During 2015-2018, the FFO to total debt ratio is expected to average around 7%, while the EBITDA interest coverage ratio will be held at 3 times or more.

Financial Statistics and Key Financial Ratios *

Unit: Bt million

		------------------------- Year Ended 31 December --------------------				
	Jan-Sep 2015	2014	2013	2012	2011	2010
Revenue	15,547	19,575	17,865	11,358	8,896	5,259
Finance cost	254	106	27	0	0	0
Net income from operations	23	497	775	482	363	319
Funds from operations (FFO)	1,088	414	825	520	362	320
Capital expenditures	81	56	81	802	78	47
Total assets	24,544	22,652	14,979	7,659	6,904	3,675
Total debts	8,857	7,391	934	0	0	0
Total liabilities	17,613	16,237	9,042	5,338	5,221	2,139
Shareholders' equity	6,930	6,415	5,937	2,321	1,682	1,536
Depreciation & Amortization	36	49	30	24	22	21
Dividends	297	392	355	216	192	166
Operating income before depreciation and amortization as a % of sales	3.04	2.38	5.57	5.48	5.48	8.23
Pretax return on permanent capital (%)	2.98 **	6.18	22.96	33.50	32.81	30.81
Earnings before interest, tax, depreciation, and amortization (EBITDA) interest coverage (times)	2.04	6.49	39.65	> 40	> 40	> 40
FFO/total debt (%)	13.04 **	5.61	88.32	> 250	> 250	> 250
Total debt to capitalization (%)	56.10	53.54	13.59	0	0	0

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

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