S&P Global Ratings

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Research Update:

Ratch Group Public Co. Ltd. 'BBB+' Rating Affirmed; Outlook Stable

December 17, 2019

Rating Action Overview

- We expect Ratch Group Public Co. Ltd.'s good cash flow visibility and increasing scale and diversity to help it withstand the impact of higher leverage over the next two years.
- We believe Ratch's capital spending will peak in 2020 as the Thailand-based power company executes its growth investments. The debt-to-EBITDA ratio will then exceed 2.5x.
- On Dec. 18, 2019, S&P Global Ratings affirmed its 'BBB+' long-term issuer credit rating on Ratch and the 'BBB+' long-term issue rating on the senior unsecured notes and U.S. dollar-denominated medium-term note program that RH International (Singapore) Corporation Pte. Ltd. (RHIS), a wholly owned subsidiary of Ratch, issued. Ratch guarantees the notes.
- The stable outlook reflects our expectation that Ratch will appropriately manage its growth aspirations and leverage over the next 24 months such that the debt-to-EBITDA ratio stabilizes at 2.5x-2.7x, after rising from our estimate of 2.0x at the end of 2019.

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Rating Action Rationale

We affirmed the rating because we believe Ratch's good cash flow visibility and growing scale will cushion the impact of an increase in leverage owing to higher capital spending and investments in offshore projects.

We believe Ratch will continue to benefit from strong earnings visibility backed by favorable power purchase agreements (PPAs) with Electricity Generating Authority of Thailand (EGAT), which is a strong counterparty. We expect the PPAs with EGAT to account for 65% of Ratch's operational equity capacity, and anticipate that availability and energy payments under the agreements will contribute 40%-50% of Ratch's adjusted EBITDA over the next one to two years. These long-term PPAs protect the company from demand-volume and fuel-cost risks, supporting earnings stability. In addition, Ratch has secured a 25-year PPA with EGAT for a 1,400 megawatt (MW) capacity project in Ratchaburi province, as part of Thailand's new Power Development Plan (PDP) 2018. In our view, earnings contribution (post its commissioning in 2024 and 2025) from this project will help offset the impact of a structural decline in availability payments from legacy independent power producer (IPP) generation plants.

Ratch's scale and diversity will likely improve steadily with continued growth in its wholly owned Australia business. The company's installed capacity in Australia will increase to 1,250 MW by the end of 2021 following the commissioning of the Collector Wind Plant and Yandin Wind Plant--representing 377MW of additional capacity. We expect Ratch's Australia operations to account for more than 30% of total EBITDA from 2021. This will support overall earnings quality, given the favorable long-term contracts with minimal volume and price risk. Tariffs and offtake volumes are fixed for about 90% of the company's Australia capacity, while the rest is exposed to the merchant market. Increasing focus on renewable energy (particularly wind power projects) will also improve Ratch's margin profile, in our view.

We anticipate Ratch's leverage will increase steadily over the next 12-24 months due to the company's growth plans and elevated spending on committed projects. We expect Ratch's debt-to-EBITDA ratio to trend close to 2.0x in 2019, and increase to about 2.6x over 2020-2021, from historical low levels of 1.3x. Capital spending for the Collector Wind Plant and planned equity infusion into affiliates (such as Yandin Wind Plant and Nuclear plant project in China) will result in peak spending for Ratch of close to Thai baht (THB) 15 billion in 2020. We believe spending will likely moderate to about THB2 billion annually thereafter as the company seeks to manage its growth aspirations beyond the planned investments. The company's capacity will likely increase to 9.3GW over the next five years, trending close to its aspirational capacity of 10GW.

We expect Ratch to exercise financial discipline, be prudent in scaling up, and not undertake investments that could further pressure its balance sheet. An improvement in leverage is likely in 2023, when dividends from affiliates stabilize and earnings from new projects come on-stream, with the debt-to-EBITDA ratio trending close to the company's target of 2.0x-2.5x.

Ratch is diversifying into infrastructure-related sectors, which could pose some risks to earnings and cash flow stability, in our view. These risks are partly offset by the company's strategy of collaborating with experienced partners with good technical capabilities, investing through minority stakes, and the limited earnings contribution from these investments (we do not expect earnings contribution from the infrastructure business to exceed more than 10% over the next five years). We also believe Ratch will prudently evaluate investments based on their earnings profile and payback period.

Outlook

The stable outlook on Ratch reflects our expectation that the company will appropriately manage its growth aspirations and leverage over the next 24 months. We expect its debt-to EBITDA ratio to be steady at 2.5x-2.7x over the period, after rising from our estimate of 2.0x at the end of 2019. We anticipate Ratch's relationship with and credit quality of its controlling shareholder, EGAT, will not materially change in the period.

Downside scenario

If the foreign currency long-term sovereign credit rating on Thailand is raised to 'A-', we would lower the rating on Ratch by one notch if the company's 'bbb+' stand-alone credit profile (SACP) falls to 'bb'.

If the foreign currency long-term sovereign credit rating on Thailand remains at 'BBB+', we may lower the rating on Ratch by one notch if the company's 'bbb+' SACP falls to between 'bbb' and 'bb'. This assumes that EGAT and the government will be incentivized to provide extraordinary financial support to Ratch in the case of its financial distress, and that the relationship between EGAT and Ratch will remain intact.

We may lower our assessment of Ratch's SACP by one notch if the company's debt-to-EBITDA ratio approaches 3x for a prolonged period. This could happen if Ratch undertakes: (1) aggressive debt-funded expansion, reflecting a change in the company's financial policy; or (2) sustained investments through joint ventures (JVs) that weaken its balance sheet. This includes cases of adverse developments at JVs where we believe Ratch will extend financial support, or a significant increase in debt on existing high-risk JV projects in which Ratch has a significant interest.

Upside scenario

We are unlikely to raise the rating on Ratch over the next two years unless our view on the group's credit profile strengthens to 'a', and Ratch maintains an SACP of 'bbb-' or higher.

Company Description

Ratch is Thailand's second-largest power generator, with operations mainly in Thailand, Australia, and Laos. The company's total operational capacity is about 7GW, including JVs. It is 45% owned by EGAT.

Our Base-Case Scenario

- Thailand and Australia's GDP growth of around 2.8% and 2.2%, respectively, in 2020, which will support power demand.
- Ratch's EBITDA, adjusted for principal repayment on financial leases and dividends from JVs, of THB10.5 billion in 2019 and THB11 billion-THB12 billion over 2020-2021.
- Dividends received from equity-accounted JVs of more than THB2.5 billion a year.
- Capital spending including investment in affiliates of about THB15 billion in 2020 and about THB2 billion in 2021.
- Adjusted debt of about THB30 billion over 2020-2021 on account of accelerated spending, from THB21 billion in 2019.
- Stable dividend payout of approximately THB3.5 billion annually.

Based on these assumptions, we arrive at the following adjusted credit measures:

- Debt-to-EBITDA ratio of close to 2.0x in 2019, increasing to about 2.6x over 2020 and 2021.
- Ratio of funds from operations (FFO) to debt of about 38% in 2019, decreasing to 30% over 2020 and 2021.

Liquidity

We assess Ratch's liquidity as adequate because we anticipate that the company's funding sources will cover uses by more than 1.2x over the next 12 months ending Sept. 30, 2020. Ratch has supportive banking relationships and good access to domestic and international debt markets, given its market position and indirect connection to the government through EGAT. We expect the company to maintain sufficient headroom in its covenants even if EBITDA declines by 15%.

Principal liquidity sources include:

- Cash and short-term investments of about THB12.5 billion as of Sept. 30, 2019.
- Undrawn long-term committed facilities of about THB3 billion.
- Cash flow from operations of about THB6 billion until Sept. 30, 2020.
- Working capital inflow of THB2 billion over the period.

Principal liquidity uses include:

- Short-term debt maturities of THB2.3 billion over the 12 months ending Sept. 30, 2020.
- Consolidated capital spending including investment in affiliates of up to THB13 billion over the period.
- Dividend payments of up to THB3.5 billion per year.

Environmental, Social, And Governance

We believe Ratch's environmental, social, and governance risks are neutral to its credit quality. The company's JV renewable energy projects in countries neighboring Thailand provide some diversification from its overdependence on gas. Ratch's foray into renewables outside Thailand can improve carbon exposure and enhance its country and fuel diversification. However, environmental and social risks for some hydro projects could be elevated as seen in its Laos JV project's dam break, which resulted in some casualties. While financially the incident had an insignificant impact on Ratch, adverse public opinion or geopolitical resistance could affect the company's growth plans. We believe Ratch has an adequate governance framework in line with peers'.

Issue Ratings - Subordination Risk Analysis

Capital structure

As of Sept. 30, 2019, Ratch's capital structure consists of about THB29.4 billion of total debt. All borrowings issued by RHIS are unsecured.

Analytical conclusions

We equalize the issue rating on Ratch's U.S. dollar medium-term note program and Japanese yen bond, both issued by RHIS, with the issuer credit rating on Ratch. Under the terms of the notes, these debts are irrevocably and unconditionally guaranteed by the rated parent.

Ratings Score Snapshot

Issuer Credit Rating: BBB+/Stable/--

Business risk: Satisfactory

- Country risk: Moderately high

- Industry risk: Moderately high
- Competitive position: Satisfactory

Financial risk: Intermediate

- Cash flow/Leverage: Intermediate

Anchor: bbb

Modifiers

- Diversification/portfolio effect: Neutral (no impact)
- Capital structure: Neutral (no impact)
- Liquidity: Adequate (no impact)
- Financial policy: Neutral (no impact)
- Management and governance: Satisfactory (no impact)
- Comparable rating analysis: Positive (+1 notch)

Stand-alone credit profile: bbb+

- Group credit profile: bbb+
- Entity status within group: Strategically important (no impact)

Related Criteria

- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments, April 1, 2019
- Criteria | Corporates | General: Reflecting Subordination Risk In Corporate Issue Ratings, March 28, 2018
- General Criteria: Guarantee Criteria, Oct. 21, 2016
- General Criteria: Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- Criteria | Corporates | General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- Criteria | Corporates | Industrials: Key Credit Factors For The Unregulated Power And Gas Industry, March 28, 2014
- Criteria | Corporates | General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Methodology: Timeliness Of Payments: Grace Periods, Guarantees, And Use Of 'D' And 'SD' Ratings, Oct. 24, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities, Nov. 13, 2012

- General Criteria: Stand-Alone Credit Profiles: One Component Of A Rating, Oct. 1, 2010
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Ratings List

Ratings Affirmed	
Ratch Group Public Co. Ltd.	
Issuer Credit Rating	BBB+/Stable/--
RH International (Singapore) Corporation Pte. Ltd.	
Senior Unsecured	BBB+