

EASTERN WATER RESOURCES DEVELOPMENT AND MANAGEMENT PLC

No. 97/2021

25 June 2021

CORPORATES

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

Last Review Date: 30/06/20

Company Rating History:

Date	Rating	Outlook/Alert
23/01/08	A+	Stable
20/09/07	A+	Alert Developing
12/07/04	A+	Stable
29/06/04	A+	-

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RATIONALE

TRIS Rating affirms the company rating on Eastern Water Resources Development and Management PLC (EASTW) and the ratings on its outstanding senior unsecured debentures at “A+”, with a “stable” outlook. The ratings reflect EASTW’s strength as a key raw water provider with a comprehensive pipeline network in the Eastern Seaboard area, its reliable cash flow, and strong profitability. These strengths are partially offset by the uncertainty of water supply caused by climate changes and its higher leveraged balance sheet.

KEY RATING CONSIDERATIONS

Key raw water provider in the Eastern Seaboard

EASTW’s position as the key provider of raw water in the Eastern Seaboard underpins its strong business profile. Its integrated pipeline network facilitates the efficient allocation and channeling of water from multiple sources to service areas in Chonburi, Rayong, and Chachoengsao provinces. EASTW’s comprehensive network makes it uneconomical for any newcomer to compete in the company’s service areas. In addition to the large capital investment needed to develop water distribution infrastructure, new pipelines require rights of way which would have to pass the approval of several government agencies.

EASTW’s water sources are another advantage. The company has the rights to access multiple sources of water, including government and privately-owned reservoirs. As of June 2021, EASTW’s water sources amounted to 430 million cubic meters (MCM) at full capacity.

Rising demand in the EEC

The company has successfully expanded its water services portfolio in the Eastern Economic Corridor (EEC) in recent years. Although raw water and tap water products accounted for 59% and 35% of total sales in 2020, industrial water and fully integrated water services are expected to contribute more in the near future.

Long-term contracts signed in 2018 with Gulf P.D. Co., Ltd. (Gulf PD) and Amata Water Co., Ltd. (Amata Water) to supply industrial water should both commence operations as planned in 2021. The company started providing services to Amata Water in January 2021 and it expects to commence services to Gulf PD in the fourth quarter of the year. These two contracts are expected to generate revenues of approximately THB100 million in 2021 and THB240 million per annum from 2022 onwards.

Another project to provide tap water, wastewater treatment, and recycled water services to U-Tapao airport is expected to commence operations in 2023.

EASTW also signed contracts with several other companies in the EEC area in 2020, including major agreements with Carabao Group PLC (CBG), Thai Oil PLC (TOP), and PTT PLC (PTT) for the supply of industrial water, raw water, and tap water at Wang Chan Valley, respectively. These services should get underway in 2021-2022.

The company is mainly focusing on expanding its service footprint in the EEC, while also seeking opportunities elsewhere.

Recovering from drought in 2021

One unpredictable factor that affects water supplies is the climate. During the dry season or in periods of drought, water sources become depleted while the cost of feeding water from distant sources increases. Apart from existing sources from the Royal Irrigation Department (RID), EASTW has developed its own reservoirs and sources of raw water from private ponds, though the cost has been relatively high.

The drought in Thailand became serious in 2019-2020, with the lowest level of rainfall in the past 10 years. The water volume of reservoirs in Chonburi and Rayong provinces fell dramatically from 2017-2018 levels, affecting EASTW's performance. EASTW's total revenue in 2020 dropped by 10% to THB4.2 billion, from THB4.7 billion in 2019. A 19% fall in raw water sales volume from 2019 was the key factor in the revenue decline.

In 2021, EASTW seems to be recovering from the drought. As of 4 June 2021, the water storage volume of EASTW's major water reserves in Chonburi and Rayong provinces stood at approximately 67% of maximum capacity, well above the 23% recorded on the same period of the previous year. TRIS Rating expects the company to have no drought issues in 2021 and water reserves should be sufficient to cover demand throughout the year.

For the first three months of 2021, EASTW's total revenue increased by 6% to THB1.2 billion. Raw water sales volume increased by 10% over the same period of 2020.

Profitability remains strong despite the decline in recent years

Strong profitability and reliable cash flow are EASTW's key strengths. Despite the drought situation in 2020, the company's earnings before interest, taxes, depreciation, and amortization (EBITDA) continued to record THB2 billion, 10% lower than the THB2.3-THB2.4 billion recorded during 2015-2019. The EBITDA margin dropped to 48%, from the 50%-55% range during 2015-2019.

New tariffs on raw water, effective from January 2021, are another factor that should help stabilize EASTW's profitability in 2021. The new structure is designed to pass-through any cost incurred to users while having incentive and penalty scheme to motivate efficiency in water usage. The tariff is indexed with changes in the consumer price index (CPI) and electricity cost and also incorporate potential rise in water resource cost associated with the Water Resource Bill 2560. The new tariff for 2021 will be 2%-3% higher than the average tariff in 2020.

With increased water levels in the company's main reservoirs in the first half of the year, we expect EASTW to see improved performance in 2021. EBITDA increased by 12% in the first quarter of 2021, from the same period in 2020.

TRIS Rating expects EASTW's revenue to increase by 11% in 2021 and 5% per annum in 2022-2023. The EBITDA margin is expected to hover around 50% throughout the forecast period. EBITDA in 2021 should bounce back to around THB2.4 billion due mainly to contributions from new clients.

Investment projects to push up leverage

Under TRIS Rating's base-case scenario, we expect EASTW's leverage to increase in 2021 then decline slightly in 2022-2023. EASTW has invested heavily to secure water supplies to cope with rising demand from its customers and to mitigate the unpredictable drought situation.

EASTW plans capital expenditure of approximately THB7 billion over the next three years. Around THB4.9 billion will be spent in 2021, of which THB3 billion has been earmarked to develop its own reservoir namely the "Tabma Project" and build a new pipeline connected to the "Klong Luang Reservoir". These two projects will increase water supply for the company by 13% from 2021 onwards.

The remaining capital expenditure will be used to upgrade pumping stations and to develop technology and facilities for total water solution projects. We expect EASTW's total debt to capitalization ratio to climb to around 50% in 2021 before declining slightly to 48% in 2023. We expect the adjusted net debt to EBITDA ratio to rise to 5 times in 2021, then gradually decline to 4.2 times in 2023.

At the end of March 2021, EASTW's leverage and liquidity profile remained sound. The total debt to capitalization ratio was healthy at 42.2%. The net debt to EBITDA ratio was 3.9 times for the first three months of 2021.

BASE-CASE ASSUMPTIONS

- Total revenues to increase by 11% in 2021, then grow by 5% per annum in 2022-2023.
- Gross profit margin to stay at 44% and EBITDA margin at 50% in 2021-2023.
- Total capital spending of THB4.9 billion in 2021, THB1.2 billion in 2022, and THB800 million in 2023.

RATING OUTLOOK

The “stable” outlook reflects our expectation that EASTW’s operations will remain resilient and continue to generate reliable streams of cashflow. TRIS Rating also expects the company to continue expanding through the conservative use of leverage and maintain its financial discipline.

RATING SENSITIVITIES

A rating upside depends on whether EASTW can materially increase operating cash flow without weakening its balance sheet. A rating downside, on the other hand, could come from overly aggressive, debt-funded investments, resulting in the debt to capitalization ratio rising above 50% on a sustained basis.

COMPANY OVERVIEW

EASTW was established in 1992 by a Cabinet resolution. The government granted EASTW a mandate to develop and manage raw water distribution systems in the Eastern Seaboard area. As of May 2021, EASTW’s major shareholders were the Provincial Waterworks Authority (PWA) (owning a 40.2% stake); Manila Water Company, Inc. (MWC; 18.7%); and the Industrial Estate Authority of Thailand (IEAT; 4.6%).

In 2020, EASTW extracted 278 MCM of raw water and supplied a total of 256 MCM, including internal use for tap water production. Currently, EASTW supplies raw water in Chonburi, Rayong, and Chachoengsao provinces. The company has a strategy to focus more on comprehensive water solutions, covering raw water, tap water, industrial water, wastewater management, and recycled water.

EASTW, through its subsidiary, Universal Utilities PLC (UU), provides tap water services in 12 areas with a total production capacity of 401,030 cubic meters (cu.m.) per day in 2020. Excluding construction revenue under concession agreements, raw water sales accounted for 60% of the company’s total revenue, while tap water services represented 36% of the total in 2020.

In 2018, EASTW signed a 25-year contract with Gulf PD and a 30-year contract with Amata Water to supply industrial water of 22 MCM per year and 5.5 MCM per year, respectively. Revenues from these industrial water contracts will be recognized from 2021 onwards.

In 2020, the company entered into four significant agreements to provide total water solutions in the EEC area: a 25-year concession to provide tap water and wastewater treatment services to U-Tapao airport; a 20-year contract for the supply of industrial water to CBG; a 30-year contract to supply tap water to PTT at Wang Chan Valley; and a 32-year contract for the supply of raw water to TOP.

KEY OPERATING PERFORMANCE

Table 1: EASTW’s Total Revenue Breakdown by Line of Business

Line of Business	Unit	2016	2017	2018	2019	2020	Jan-Mar 2021
Raw water	%	62	57	57	61	59	65
Tap water	%	32	33	34	32	35	29
Industrial water	%	-	-	-	-	-	0.4
Engineering services and rental	%	4	4	4	3	3	4
Construction revenue under concession agreement	%	3	6	6	4	3	2
Total	%	100	100	100	100	100	100
Revenue from sale & service	Mil. THB	4,377	4,308	4,221	4,680	4,204	1,231

Source: EASTW

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS*

Unit: Mil. THB

	Jan-Mar 2021	-----Year Ended 31 December -----			
		2020	2019	2018	2017
Total operating revenues	1,238	4,218	4,701	4,235	4,335
Earnings before interest and taxes (EBIT)	501	1,138	1,472	1,542	1,666
Earnings before interest, taxes, depreciation, and amortization (EBITDA)	732	2,038	2,317	2,297	2,353
Funds from operations (FFO)	592	1,574	1,822	1,802	1,812
Adjusted interest expense	54	256	232	234	240
Capital expenditures	385	1,609	1,527	796	849
Total assets	24,641	22,854	21,181	20,141	19,483
Adjusted debt	8,354	8,552	7,161	6,511	7,131
Adjusted equity	11,442	11,069	11,014	10,805	10,430
Adjusted Ratios					
EBITDA margin (%)	59.10	48.31	49.28	54.23	54.28
Pretax return on permanent capital (%)	5.85 **	5.88	8.00	8.54	9.23
EBITDA interest coverage (times)	13.60	7.95	9.97	9.80	9.82
Debt to EBITDA (times)	3.95 **	4.20	3.09	2.83	3.03
FFO to debt (%)	19.57 **	18.40	25.44	27.67	25.41
Debt to capitalization (%)	42.20	43.59	39.40	37.60	40.61

* Consolidated financial statements

** Annualized from the trailing 12 months

RELATED CRITERIA

- Issue Rating Criteria, 15 June 2021
- Rating Methodology – Corporate, 26 July 2019
- Key Financial Ratios and Adjustments, 5 September 2018

Eastern Water Resources Development and Management PLC (EASTW)

Company Rating:	A+
Issue Ratings:	
EASTW226A: THB1,200 million senior unsecured debentures due 2022	A+
EASTW256A: THB1,200 million senior unsecured debentures due 2025	A+
Rating Outlook:	Stable

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