FitchRatings

RATING ACTION COMMENTARY

Fitch Affirms Eastern Polymer Group at 'A-(tha)'; Stable Outlook

Thu 26 Aug, 2021 - 3:24 AM ET

Fitch Ratings - Bangkok - 26 Aug 2021: Fitch Ratings (Thailand) Limited has affirmed Eastern Polymer Group Public Company Limited's (EPG) National Long-Term Rating and the National Long-Term Rating on its senior unsecured debt at 'A-(tha)'. The Outlook is Stable.

EPG's rating reflects its steady operating performance amid the economic downturn, its leading position in a niche market through diversified businesses and low leverage. On the other hand, the rating is constrained by its small operating scale compared with higher-rated peers.

KEY RATING DRIVERS

Pre-Pandemic Revenue in FY22: Fitch expects EPG's revenue to return to pre-pandemic levels by the year ending March 2022 (FY22) due to improving export sales in its automotive-related and insulation businesses, driven by a global economic recovery. Its new US insulation plant will add capacity, raising revenue. The recovery in local light commercial vehicle production (6M21: 0.5 million units or 90% of 2019 level) will also support growth momentum for its Thai automotive business. EPG's 1QFY22 sales rose 50% yoy, or 8.9% qoq, to THB2.9 billion.

Strong Financial Profile: EPG's credit metrics are solid for its rating. Its net financial leverage - measured by funds from operations (FFO) net leverage - is likely to remain below 1.0x in FY22-FY24, while we project FFO fixed-charge coverage to be above 8x. Operating cash flows are likely to cover planned capex with some headroom for additional investments. Its maintenance capex is low at THB100 million.

Steady Cash Flow: EPG performed better than we expected in the pandemic on lower raw material costs and higher-than-expected sales. Revenue fell 6% in FY21, less than our forecast 17% drop, led by the rapid recovery of the automotive parts and accessories business after a temporary disruption in auto production in 1QFY21, and improving operations in Australia. We believe EPG benefits from its exposure to light commercial vehicles, which is more resilient to downturns than passenger vehicles. We expect FFO of THB1.6 billion-1.9 billion in FY22-FY24.

Manageable Profitability: We expect EPG's FY22 EBITDA margin to remain sound at around 17%, despite higher polymer costs (40%-55% of total production costs), on lower operating costs from the US insulation plant's higher efficiency and the Australian automotive accessories unit's better margins. Effective inventory management and ability to pass on higher raw material costs to automotive and insulation customers will also help its margin. Its 1QFY22 EBITDA margin widened to 19.2% in 1QFY22 from 17.9% in 4QFY21 on higher average selling prices and lower freight costs.

Niche Market Position: EPG is the leading automotive parts manufacturer in Thailand. It pioneered a no-drilling installation technology for truck-bed liners, helping it become the market leader in truck-bed liners in Thailand. EPG is also the first to produce a patented double-shell acrylonitrile butadiene styrene (ABS) alloy canopy used on pick-up trucks. ABS is the only plastic acceptable to original equipment manufacturers (OEM), giving EPG a first-mover advantage.

EPG is also the global market leader in ethylene propylene diene monomer (EPDM) rubber insulation, accounting for about 8%-11% of the worldwide market for synthetic rubber insulation. The market is, however, dominated by nitrile butadiene rubber (NBR) insulation, which accounts for around 90% of the share. NBR has been in the market far longer and is more widely used and cheaper than EPDM.

End-Market Diversification: EPG's automotive parts and accessories made up 47% of total revenue in FY21, thermal insulation 27%, and food and beverage plastic packaging 26%. The diversification helped to mitigate sector-specific risks, such as the cyclicality of the automotive and construction industries, and the low barriers to entry and intense competition of the food and beverage plastic-packaging industry. EPG's businesses have synergies in terms of raw-material sourcing and R&D as it uses polymer and plastic compounds for all its products.

Geographically Diverse Customers: EPG sells 50%-60% of its automotive parts and accessories to leading global automakers as an original design manufacturer (ODM) and OEM, while the rest is sold to automobile dealers in Thailand and another 100 countries under its own brand. About 30% of its thermal insulation sales are in Thailand, of which half are directly to construction projects.

EPG has production plants in the US to support its offshore sales, and has licensed two plants in Russia and India to make its products. About 90% of its rigid plastic-packaging products are sold in Thailand, of which about 40% are to leading food and beverage companies.

DERIVATION SUMMARY

EPG's business profile is moderate relative to that of Thai national peers, but its financial profile is stronger. EPG's peers in the polymer and plastic-product business include Polyplex (Thailand) Public Company Limited (PTL, A-(tha)/Stable), one of the 10 largest polyethylene terephthalate, or PET, film producers in the world by output, although they are in different end-user segments. EPG's operations are less geographically diversified, but serve more end-markets and products, which counterbalance its smaller operating scale. Both companies also have low financial leverage, with FFO net leverage of below 1.0x. Therefore, they have the same ratings.

EPG can be compared with KCE Electronics Public Company Limited (A-(tha)/Stable), one of the world's top-10 automotive printed circuit board (PCB) producers by revenue. KCE operates in a higher-risk industry, component electronics, but this is offset by KCE's focus on the niche segment of automotive PCBs, which has higher barriers to entry. KCE and EPG have comparable operating scales, but KCE has better EBITDA and free cash flow (FCF) margins. Their ratings are the same due to their comparable business profiles and similarly low financial leverage.

EPG has higher revenue and EBITDA than JWD InfoLogistics Public Company Limited (BBB-(tha)/Stable), one of the dominant players providing full-service inland logistics services in Thailand. JWD has higher revenue visibility, supported by a concession and medium-to-long term contracts but EPG has greater geographical diversification. Their customers are also diversified by industry. JWD's rating also reflects our expectation of high investments and sustained negative FCF, resulting in weaker deleveraging ability. EPG has much stronger cash flows and leverage, and hence, has a higher rating.

KEY ASSUMPTIONS

Fitch's Key Assumptions Within Our Rating Case for the Issuer

- Revenue growth at 7%-8% per annum in FY22-F23, supported by recovery demand in thermal insulation and automotive parts and accessories businesses, and volume growth from additional capacity in thermal insulation business.

- Operating EBITDA margin of about 17% (FY21: 17.9%; 1QFY22: 19.2%)

- Capex to total THB2.1 billion during FY22-FY24

- 70% dividend payout ratio

RATING SENSITIVITIES

Factors that could, individually or collectively, lead to positive rating action/upgrade:

- We do not expect positive rating action in the next 24 months due to EPG's smaller operating scale compared with higher-rated peers

Factors that could, individually or collectively, lead to negative rating action/downgrade:

- Lower cash flow or higher investments than Fitch expects, leading to FFO net leverage sustained above 1.5x

- A weakening in business profile or competitive position, reflected in a sustained decline in funds flow from operations

LIQUIDITY AND DEBT STRUCTURE

Sound Liquidity: EPG's liquidity is supported by its cash and cash equivalents of THB1.3 billion as of end-June 2021. Debt maturing over the next 12 months amounts to THB0.9 billion, of which about 94% is short-term debt used mainly for working capital. EPG had available uncommitted working-capital facilities of THB6.0 billion at end-June 2021. Fitch expects the company to be able to roll over its short-term debt, supported by a healthy credit profile.

ISSUER PROFILE

EPG is a leading manufacturer of EPDM rubber insulation, polymer and plastic automotive parts and accessories, and disposable rigid plastic packaging for food and beverage. EPG generates about 45% of its revenue from the domestic market and 55% from overseas, with Australia and the US contributing around 20% and 10%, respectively, with the remainder from Asia and Europe.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

RATING ACTIONS

ENTITY/DEBT	RATING			PRIOR
Eastern Polymer Group Public Company Limited	Natl LT	A-(tha) Rating Outlook Stable	Affirmed	A-(tha) Rating Outlook Stable
• senior unsecured	Natl LT	A-(tha)	Affirmed	A-(tha)

VIEW ADDITIONAL RATING DETAILS

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APPLICABLE CRITERIA

Corporate Rating Criteria (pub. 21 Dec 2020) (including rating assumption sensitivity)

National Scale Rating Criteria (pub. 23 Dec 2020)

Corporates Recovery Ratings and Instrument Ratings Criteria (pub. 09 Apr 2021) (including rating assumption sensitivity)

Sector Navigators - Addendum to the Corporate Rating Criteria (pub. 01 May 2021)

APPLICABLE MODELS

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

Corporate Monitoring & Forecasting Model (COMFORT Model), v7.9.0 (1)

ADDITIONAL DISCLOSURES

Solicitation Status

Endorsement Policy

ENDORSEMENT STATUS

Eastern Polymer Group Public Company Limited	-

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Corporate Finance   Industrials and Transportation   Asia-Pacific   Thailand

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