FitchRatings

30 AUG 2023

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

Fitch Ratings - Bangkok - 30 Aug 2023: Fitch Ratings (Thailand) 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.

The affirmation reflects EPG's strong financial profile despite a temporary increase in EBITDA net leverage from the acquisition of Australia-based 4 Way Suspension Products Pty. Ltd. (4WS) in July 2022. Fitch expects EPG's leverage to remain low in the medium term, despite temporarily weaker earnings in the financial year ended March 2023 (FY23). The company's rating is constrained by its smaller operating scale than that of higher-rated peers.

Key Rating Drivers

Leverage to Improve: EPG's EBITDA net leverage is likely to improve gradually to below 1.0x in FY25-FY28 from 1.3x in FY23. EPG does not have a large committed capex plan in the next three years, as its existing production capacity is adequate to support growth in the medium term. Fitch does not forecast any major acquisitions in the medium term because we believe EPG will prioritise value creation from the 4WS acquisition through synergies with its existing businesses. As a result, we expect EPG to generate positive free cash flow during FY24-FY28.

Revenue to Rise: Fitch expects EPG's sales to continue to grow at a mid-single digit rate over the medium term (FY23: 3%), supported by the full-year consolidation of 4WS. EPG's sales growth in the automotive parts and packaging businesses slowed temporarily in 1QFY24 due to a delay in automobile deliveries in Australia, and weaker buyer sentiment amid signs of a looming recession, which weighed on the post-pandemic recovery of the automotive industry and demand for plastic food packaging.

However, we believe revenue will pick up starting 2HFY24 as the automotive parts and insulation business should benefit from an easing in the global micro-chip shortage and the introduction of new models of pickup trucks by leading automakers. Higher demand for insulation products from industrial customers, especially those related to semiconductor and electric-vehicle businesses, would also support growth.

Profitability to Rebound: We forecast EPG's EBITDA margin will improve in the medium term on our expectation of a decline in raw-material prices in line with crude oil, a ramp-up in capacity utilisation at its newly commissioned manufacturing facility in the US, and our belief the company will benefit from synergies at 4WS. EPG's EBITDA margins will soften to around 14% in FY24 (FY23: 15%, FY20-FY22:

16%-18%) due to higher operating costs, particularly from higher overheads at the US plant, and 4WS in Australia.

Diversity Across Products, End-Uses: EPG's products are diversified across end-uses, including auto parts, insulation and packaging. This helps to mitigate sector-specific risks, such as the cyclicality of the automotive and construction industries, and the low barriers to entry and intense competition in the food and beverage plastic-packaging industry. EPG's businesses have synergies in terms of raw-material sourcing and R&D. EPG's acquisition of 4WS further diversifies its automotive product portfolio, in addition to its existing polymer-based products.

Geographically Diverse Customers: EPG sells 50%-60% of its automotive parts and accessories to leading global automakers as an original design or equipment manufacturer, while the rest is sold to automobile dealers in Thailand and another 100 countries under its own brand. About 25% of its thermal insulation sales from its main plants in Thailand and the US are in Thailand, of which half are directly to construction projects. About 90% of its rigid plastic-packaging products are sold locally, of which about 40% are to leading food and beverage companies.

Feedstock Price Volatility: EPG is vulnerable to fluctuations in raw-material prices, mainly polymers and plastic beads, which account for 40%-50% of the cost of goods sold. These polymer prices are driven by their petrochemical feedstock prices, which are determined largely by crude oil prices. A substantial rise in polymer prices may cause a temporary and material deterioration in EPG's margins and profitability.

However, EPG has historically been able to pass on rising costs to customers after a lag of around two months as its automotive parts and accessories, and thermal insulation products have few competitors, while the packaging business can increase prices at a faster pace for its retail customers.

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. 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. Their financial leverage is relatively low but we expect the ratio to rise temporarily from their increased capex and investments.

EPG is rated higher than Bangkok Aviation Fuel Services Public Company Limited (BAFS, BBB+(tha)/Negative) given EPG's stronger financial profile with low leverage. EPG also has more diversified products, serves broader end-user segments and operates in more geographically diversified locations than BAFS, which operates the fuel depot, hydrant system and fueling service in Thailand's airports.

Key Assumptions

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

- Revenue growth of 4%-5% during FY24-FY28

- Operating EBITDA margin of about 14%-17% (FY23: 14.8%; 1QFY24: 15.0%)

- Total capex of about THB600 million per year

- Dividend payout ratio of approximately 60%

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 than that of 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 EBITDA net leverage sustained above 1.5x

- A weakening in business profile or competitive position, reflected in a sustained decline in EBITDA

Best/Worst Case Rating Scenario

International scale credit ratings of Non-Financial Corporate issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of four notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit https://www.fitchratings.com/site/re/10111579.

Liquidity and Debt Structure

Manageable Liquidity: EPG's liquidity is supported by its cash and cash equivalents of THB1.3 billion as of end-March 2023. Debt maturing over the next 12 months amounts to THB1.5 billion, of which about 84% is short-term debt used mainly to support working capital. EPG had available uncommitted working-capital facilities of THB4.6 billion at end-March 2023. We believe EPG's liquidity is also supported by its healthy access to domestic banks in light of its good operational record and healthy credit profile.

Issuer Profile

EPG is a leading manufacturer of ethylene propylene diene monomer rubber insulation, polymer and plastic automotive parts and accessories, and food and beverage plastic packaging. The automotive parts and insulation businesses contributed around 49% and 30% of total group revenue in FY23, respectively. The plastic packaging business made up the remainder.

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.

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Rating Actions

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

RATINGS KEY	OUTLOOK	WATCH
POSITIVE		
NEGATIVE		
EVOLVING		
STABLE		

Applicable Criteria

Corporate Rating Criteria (pub.28 Oct 2022) (including rating assumption sensitivity)

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

National Scale Rating Criteria (pub.22 Dec 2020)

Sector Navigators: Addendum to the Corporate Rating Criteria (pub.12 May 2023)

Applicable Models

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

Corporate Monitoring & Forecasting Model (COMFORT Model), v8.1.0 (1)

Additional Disclosures

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Endorsement Status

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