

Research Update:

# EGAT International Co. Ltd. Outlook Revised To Positive; 'BBB+' Rating Affirmed

December 11, 2019

## Rating Action Overview

- S&P Global Ratings today revised the rating outlook on Thailand to positive from stable.
- We are revising our outlook on EGAT International Co. Ltd. (EGATi) to positive from stable, following the sovereign rating action. At the same time, we are affirming our 'BBB+' long-term issuer credit rating on the company.
- EGATi operates as the investment arm for its parent Electricity Generating Authority of Thailand (EGAT) on behalf of the Thai government. We view EGATi as a core subsidiary of EGAT, and expect the company to benefit from extremely high government support via its parent.
- The positive outlook on EGATi reflects the positive outlook on the long-term sovereign credit rating on Thailand. It also reflects our expectation that EGATi will remain a core subsidiary of EGAT and continue to receive support from the government through the parent over the next 12-18 months.

### PRIMARY CREDIT ANALYST

**Cheng Jia Ong**  
Singapore  
(65) 6239-6302  
chengjia.ong  
@spglobal.com

### SECONDARY CONTACT

**Abhishek Dangra, FRM**  
Singapore  
(65) 6216-1121  
abhishek.dangra  
@spglobal.com

## Rating Action Rationale

The outlook revision on EGATi follows our sovereign rating action on Thailand. The rating on EGATi reflects our assessment of EGAT's credit profile because we consider EGATi to be a core member of the EGAT group.

EGAT's essential role as the sole transmission services provider in Thailand, the entity's dominance in power generation, and the transparent and stable regulatory framework in Thailand should support its solid earnings profile and moderate leverage.

We view EGATi as an extension of EGAT. All of EGATi's management, operations, capital expenditure (capex) funding, and investments are largely approved by EGAT, and Thailand's Ministry of Finance, Ministry of Energy (MOE), and Cabinet. We believe EGATi has an extremely high likelihood of extraordinary support from the Thai government if needed. The government supports EGATi via equity infusions from EGAT or the Cabinet-approved budget for EGATi.

We expect EGAT to maintain its dominant role in Thailand's power market and its leverage to remain moderate over the next 12-24 months. A transparent and stable regulatory framework

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supports EGAT's solid earnings profile. We also believe that EGAT will have an extremely high likelihood of extraordinary support from the government in case of need. However, EGAT is smaller than most of its rated peers in the region and does not enjoy diversification benefits. Its transmission and generation assets are only based in Thailand and generation is overdependent on gas.

In our view, the Thai government has satisfactory oversight of EGAT, and would provide timely support to the entity to deliver on its public service obligation of providing stable electricity supply. EGAT is a wholly owned government entity with active government involvement via the MOE in terms of supervision, strategy, operations, funding, and financial management. Under the Electricity Generating Authority of Thailand Act, the government is obligated to cover any deficiencies in EGAT's cash flows, including debt repayments and interest expenses. The government's obligation to prevent a financial crisis reinforces our expectation of continued majority ownership by the government.

Thailand's transparent and stable regulatory framework should continue to support EGAT's ability to generate predictable revenue and earn reasonable returns on investments. The Energy Regulatory Commission (ERC) regulates electricity tariffs. Significant changes to the regulatory framework are unlikely, given ERC's established tariff-setting philosophy. We expect the regulator to remain generally supportive of utilities in Thailand, which supports low volatility in cash flows from these utilities.

We see high cash flow visibility for EGAT over the next few years because the entity's revenue is underpinned by regulated earnings. In addition, EGAT's financial profile will likely remain stable over the next few years supported by a strong balance sheet.

## **Outlook**

The positive outlook on EGATi reflects the positive outlook on the long-term sovereign credit rating on Thailand. It also reflects our expectation that EGATi will remain a core member of the EGAT group and continue to receive support from the Thai government through EGAT over the next 12-18 months.

The outlook also reflects our expectation that EGAT will continue to benefit from ongoing and extraordinary government support.

## **Upside scenario**

We will raise the rating on EGATi if the foreign currency long-term sovereign credit rating on Thailand is raised to 'A-'.

We could also raise the rating on EGATi if we upgrade EGAT, and EGATi remains a core subsidiary of the group and continues to receive support from the government through EGAT. This will also require a raising of the foreign currency sovereign credit rating on Thailand. Our assessment of EGAT's stand-alone credit profile (SACP) could improve if the entity's cash flows strengthen such that the ratio of funds from operations (FFO) to debt is above 35% on an ongoing basis.

## **Downside scenario**

We may revise the outlook on EGATi to stable if we revise the outlook on the long-term sovereign credit rating on Thailand.

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We could lower the rating on EGATi if we see signs of a loosening of the company's ties with its parent, or if our assessment of government support for EGATi is lower, both of which we view as unlikely in the next 12-24 months.

We could lower the rating on EGAT if its SACP falls by more than four notches.

We may lower our assessment of EGAT's SACP by one notch if: (1) the entity departs significantly from its role as the sole transmission network provider and dominant electricity generator under the "enhanced sole buyer" model, which could weaken our assessment of EGAT's business operations and quality of earnings; or (2) Thailand's regulatory framework has any significant adverse change; or (3) EGAT's cash flow adequacy deteriorates substantially, with the ratio of FFO to debt falling below 23%.

## Company Description

EGATi is the sole energy and power investment platform for international expansion under EGAT. EGAT is wholly owned by the Thai government and is the sole electricity transmission service provider and the largest electricity generator in the country.

## Our Base-Case Scenario

- Thailand's GDP to grow 2.8% in fiscal 2020 (year ending Dec. 31), with power consumption potentially lagging, given the high level of electrification and high reserve margins.
- EGAT's revenue growth to be 6.0%-8.5% over fiscals 2019-2020. Given overcapacity, we expect EGAT's revenue growth to slightly lag the country's demand forecast in the Power Development Plan (PDP).
- Gross margins to remain stable in the mid-20% range.
- Capex to be generally based on the PDP's power generation target of about Thai baht (THB) 43 billion in fiscal 2019 and moderating to THB30 billion-THB36 billion over fiscals 2020-2021.
- Average cost of funding to be about 4%.
- Dividend payout to be THB20 billion-THB24 billion annually in fiscals 2019-2020.

Based on these assumptions, we arrive at the following credit measures over the next two years:

- EBITDA margin of about 23%.
- Ratio of FFO to debt of about 28% in fiscal 2019, increasing to 31% in fiscal 2020.
- Debt-to-EBITDA ratio of 2.2x-2.4x over the period.

## Liquidity

In our view, EGATi's liquidity and funding are dependent on EGAT. We assess EGAT's liquidity as strong and forecast that the entity's sources of funds will cover its needs by more than 1.5x until end-September 2020. We believe net sources would be sufficient to cover uses even if EGAT's EBITDA declined by 30%. In addition, EGAT benefits from generally prudent risk management, well-established relationships with banks, and a generally high standing in credit markets through bond issuances.

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Principal liquidity sources include:

- Cash and cash equivalents of about THB75 billion as of Sept. 30, 2019.
- Operating cash flows of about THB90 billion until end-September 2020.

Principal liquidity uses include:

- Debt repayment of about THB30 billion until Sept. 30, 2020.
- Capex of THB35 billion annually over the next two years. This is in line with the PDP's power generation target.
- Dividends of THB20 billion-THB23 billion annually over the same period.

## Related Criteria

- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments, April 1, 2019
- 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
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- Criteria | Corporates | Utilities: Key Credit Factors For The Regulated Utilities Industry, Nov. 19, 2013
- Criteria | Corporates | General: Corporate Methodology, Nov. 19, 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; Outlook Action

	To	From
<b>EGAT International Co Ltd.</b>		
Issuer Credit Rating	BBB+/Positive/--	BBB+/Stable/--

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at [www.standardandpoors.com](http://www.standardandpoors.com) for further information. Complete ratings information is available to subscribers of RatingsDirect at [www.capitaliq.com](http://www.capitaliq.com). All ratings affected by this rating action can be found on S&P Global Ratings' public website at [www.standardandpoors.com](http://www.standardandpoors.com). Use the Ratings search box located in the left column.

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