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## Research Update:

# EGAT International Co. Ltd. Assigned 'BBB+' Rating; Outlook Stable

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## Research Update:

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## Overview

- EGATi operates as the investment arm for its parent EGAT on behalf of the Thailand government. We view EGATi as an extension of EGAT and a core subsidiary. EGATi is likely to benefit from an extremely high support from the Thailand government via its parent.
- 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 EGAT's solid earnings profile and moderate leverage.
- We are assigning our 'BBB+' long-term issuer credit rating to EGATi.
- The stable outlook on EGATi over the next 12-18 months reflects the outlook on EGAT, and our expectation that EGATi will remain a core member of the group and continue to receive support from the government through the parent.

## Rating Action

On Dec. 20, 2018, S&P Global Ratings assigned its 'BBB+' long-term issuer credit rating to EGAT International Co. Ltd. (EGATi). The outlook is stable.

EGATi is the sole energy and power investment platform for international expansion under Electricity Generating Authority of Thailand (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.

## Rationale

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.

We view EGATi as an extension of EGAT. All 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

leverage to be moderate over the next 12-24 months. A transparent and stable regulatory framework supports EGAT's solid earnings profile. We also believe that the likelihood of extraordinary government support to EGAT is extremely high. 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 over dependent on gas.

A disruption in EGAT's operations, which could be triggered by financial difficulties, is likely to have major social, economic, and political implications. The entity is also the sole purchaser of electricity from other generators, to supplement its own supply. We expect EGAT to maintain its strong market position due to its "enhanced sole buyer" model.

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 obligations of providing a 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 the low volatility in cash flows from these utilities.

EGAT's revenues are protected from increases in fuel and power purchase costs, because the entity passes on such increases to its customers. However, the implementation of tariff revisions is not automatic, and requires the approval of a government-appointed review committee.

We note that EGAT is obligated to pay for electricity from other power producers as part of its power purchase agreements, notwithstanding high reserve margins in Thailand. We have factored these obligations in EGAT's total debt.

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.

We believe execution risk is manageable for EGAT, given its stable record in operations and handling major capex. We do not expect material capital spending over the next few years because the actual capex over the last few

years was lower than we anticipated.

We could proportionally consolidate additional debt for EGAT should we assess the likelihood of EGAT providing support to the joint-venture projects of its subsidiaries or associated companies, such as EGATi and Ratchaburi Electricity Generating Holding Public Co. Ltd.

Our base case assumes:

- Average GDP growth in Thailand of 3.8% in fiscal 2019 (year ending 31 December) and 3.7% in fiscal 2020, with power consumption potentially lagging, given the high level of electrification and high reserve margins.
- EGAT's revenue growth to be 6% in fiscal 2018, primarily driven by rising fuel costs. Growth to average around 3% for fiscal 2019-2020. Given overcapacity, we expect EGAT's revenue growth to slightly lag the country's demand forecast in the Power Development Plan (PDP).
- The entity's gross margins to remain stable in the mid-20%.
- Its capex to be generally based on the PDP's power generation target at about Thai baht (THB) 55 billion-THB60 billion annually.
- Its average cost of funding to be about 4%.
- Its dividend payout to be THB25 billion-THB28 billion annually in fiscals 2018-2019.

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

- EBITDA margin of about 23%.
- Ratio of funds from operations (FFO) to debt of just over 25%.
- Debt-to-EBITDA ratio of 2.5-2.7x.

## **Liquidity**

We believe EGATi's liquidity and funding is dependent on EGAT. We assess EGAT's liquidity as adequate. We forecast that the entity's sources of funds will cover its needs by about 1.5x until the end of September 2019, and we believe net sources would be sufficient to cover uses even if EGAT's EBITDA declines by 15%. In addition, EGAT benefits from generally prudent risk management, well-established relationships with banks, and a generally satisfactory standing in credit markets. The entity has access to capital markets via the issuance of its bonds.

Principal liquidity sources:

- Cash and cash equivalents of about THB80 billion as of Sept. 30, 2018; and
- Operating cash flows of around THB80 billion until the end of September 2019.

Principal liquidity uses:

- Debt repayment of around THB35 billion until Sept. 30, 2019;

- Capex of THB55 billion-THB65 billion annually over the next two years;
- Dividends of about THB20 billion annually over the same period.

## **Outlook**

The stable outlook on EGATi reflects the outlook on EGAT and our expectation that EGATi will remain a core member of the group and continue to receive support from the Thailand government through EGAT.

The outlook also reflects our expectation that EGAT will continue to benefit from ongoing and extraordinary government support, and generate predictable cash flows with a ratio of FFO to debt of just over 25%.

### **Downside scenario**

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 support from the government for EGATi is lower, both of which we view as unlikely in the next 12-24 months.

We may also lower the rating on EGATi if we downgrade EGAT, which could happen if we lower the sovereign credit rating on Thailand (foreign currency BBB+/Stable/A-2; local currency A-/Stable/A-2).

We could lower the rating on EGAT if its stand-alone credit profile (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%.

### **Upside scenario**

We are unlikely to upgrade EGATi in the next 12-24 months, given the rating on EGAT is equalized to the foreign currency sovereign rating on Thailand.

However, over the longer term, we could 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 rating on Thailand. Our assessment of EGAT's SACP could improve if the entity's cash flows improve such that the ratio of FFO to debt above 35% on an ongoing basis.

## Related Criteria

- General Criteria: Use Of CreditWatch And Outlooks - September 14, 2009
- General Criteria: Rating Government-Related Entities: Methodology And Assumptions - March 25, 2015
- Recommended General Criteria: Group Rating Methodology - November 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions - November 19, 2013
- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments - November 19, 2013
- Criteria - Corporates - Utilities: Key Credit Factors For The Regulated Utilities Industry - November 19, 2013
- Criteria | Corporates | General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers - December 16, 2014
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers - November 13, 2012
- Criteria | Corporates | General: Corporate Methodology - November 19, 2013
- General Criteria: Methodology: Industry Risk - November 19, 2013
- General Criteria: Stand-Alone Credit Profiles: One Component Of A Rating - October 01, 2010

## Ratings List

New Rating

EGAT International Co Ltd.

Issuer Credit Rating

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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