S&P Global Ratings

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Research Update:

PTT LC Rating Outlook Revised To Negative On Industry Headwinds; FC Rating Outlook Revised To Stable; Ratings Affirmed

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Rating Action Overview

- Thailand-based PTT Public Co. Ltd. (PTT) has demonstrated its ability to preserve cash over an industry cycle.
- However, the current unprecedented industry headwinds call for drastic measures for the integrated energy company to maintain its leverage below 2.0x by 2021.
- On April 14, 2020, S&P Global Ratings revised its local currency (LC) rating outlook on PTT to negative from stable, and the foreign currency (FC) rating outlook to stable from positive. At the same time, we affirmed our 'A-' LC and 'BBB+' FC issuer credit ratings on PTT. We also affirmed our 'BBB+' long-term issue rating on the company's issued and guaranteed U.S. dollar-denominated senior unsecured notes.
- The negative outlook on the LC rating reflects our view that it will be difficult for PTT to preserve its modest leverage. The stable outlook on the FC rating mirrors that on the sovereign credit rating on Thailand.

Rating Action Rationale

We revised the outlook on the LC rating because the unusually unsupportive economic environment will weigh on PTT's earnings, while the company progresses on strategic investments. To that extent, it may be difficult for the company to preserve its modest leverage. We revised the outlook on the FC rating on PTT to stable from positive following a similar rating action on the sovereign credit ratings on Thailand (FC: BBB+/Stable/A-2; LC: A-/Stable/A-2). We affirmed the ratings on PTT because we see the company's relationship with the government of Thailand as strong and intact, supporting PTT's credit quality.

Times ahead are highly uncertain and will weigh on earnings. We see continued pressure on PTT's EBITDA, which has already contracted by 18% to Thai baht (THB) 289 billion in 2019. We now forecast the company's EBITDA to be THB250 billion in 2020 and THB280 billion in 2021.

We previously expected upstream subsidiary PTT Exploration and Production Public Co. Ltd. (PTTEP)'s volume growth to support the group's EBITDA toward THB300 billion. Collapsing oil prices have drastically undermined the company's earnings over the next two years, shaving off up to US$2 billion in EBITDA in the period compared to our estimates at the start of the year.

Likewise, other group subsidiaries will feel the pain too. We expect demand disruption will hurt the earnings of commodity chemicals producer PTT Global Chemical Public Co. Ltd. (PTTGC) and refiner Thai Oil Public Co. Ltd. at least over the next 12 months. Cancellation of flights and limited travel due to the COVID-19 pandemic have curbed demand for jet fuel, diesel, and gasoline in the first quarter of 2020. A likely global recession could further hinder demand for petroleum distillates, and consequently refining product spreads. In addition, industrywide overcapacity will continue to pressure petrochemical spreads in 2020-2022.

The earnings of PTT's other operations in natural gas and hydrocarbon marketing could be lower on weaker demand for fuels.

PTT could drastically revise its budgeted investments. The company has a track record of adjusting spending when needed. We estimate that if capital expenditure (capex) does not exceed THB380 billion over 2020-2021, the company's debt-to-EBITDA ratio could be at or below 2.0x in 2021.

Still, capex could remain sticky in 2020 at least. That is given Thai Oil's continued progress on its US$4.7 billion clean fuel project, PTTEP's investments in volume growth, and PTTGC's completion of its naphtha cracker in Map Ta Phut and propylene oxide and polyols chemicals plant.

On Dec. 31, 2019, the group had THB331 billion in cash (a reduction of THB104 billion year-on-year), financial debt of THB659 billion (THB115 billion increase), and adjusted debt of THB547 billion. Its ratio of adjusted debt to EBITDA was 1.9x. We now forecast adjusted debt at THB600 billion in 2020 and THB580 billion in 2021, and the debt-to-EBITDA ratio at 2.2x in 2020 and 2.0x in 2021.

Any slippage in operating performance below our current estimates will call for additional operating expenses, capex, or dividend reduction to protect PTT's balance sheet.

Outlook

The negative outlook on the LC rating reflects our view that it will be hard for PTT to preserve its modest leverage. The stable outlook on the FC rating on PTT mirrors that on the sovereign credit ratings on Thailand.

Downside scenario

We may lower the LC rating on PTT if we lower the sovereign LC rating on Thailand or revise downward PTT's stand-alone credit profile (SACP) by one notch to 'bbb'. We could lower the SACP if: (1) PTT's consolidated capital structure weakens, with the debt-to-EBITDA ratio exceeding 2.0x; or (2) we believe that a reducing scope of fully owned strategic assets has permanently impaired the company's earnings quality.

We may lower the FC rating on PTT if we lower the sovereign FC rating on Thailand by one notch or, in a highly unlikely scenario, PTT's SACP weakens by more than five notches.

Upside scenario

We may revise the outlook on the LC rating to stable if PTT implements cash preservation measures to protect its balance sheet against the current economic downturn, such that its debt-to-EBITDA ratio does not exceed 2.0x in 2021 and beyond.

We could raise the FC rating on PTT if we raise the FC rating on Thailand by a notch.

Company Description

PTT is an integrated energy company domiciled and operating mostly in Thailand. The company is involved in upstream oil and gas production. It generated EBITDA of THB289 billion (US$9.3 billion) in 2019 across petroleum exploration and production (47%), natural gas separation and transmission (24%), petrochemicals and refining (16%), and oil marketing, trading and others (13%). Thailand's Ministry of Finance owns 51.1% of PTT.

Our Base-Case Scenario

- Thai GDP growth of negative 2.5% in 2020 followed by a recovery of 7.6% in 2021, yet with less certain demand for petrochemicals, gas, and refined petroleum products in 2020 at least because of the COVID-19 outbreak.
- Average Brent crude price of US$30 per barrel (bbl) in 2020, US$50/bbl in 2021, and US$55/bbl thereafter, and average gas prices of below US$5.5 per mmbtu (million British thermal units) over the period.
- The peak of capacity addition to worsen the oversupply situation in petrochemicals in 2020. Demand and supply imbalances could especially weigh on high-density polyethylene (HDPE) and linear low-density polyethylene (LLDPE), while low-density polyethylene (LDPE) could see less impact from new capacity. Additional capacity from China and low-cost plants in the U.S. to likewise pressure propylene spreads, while polypropylene to face additional capacity in 2021-2023. Paraxylene and benzene spreads to soften driven by oversupply in the medium term.
- Lower pricing and volume growth in the gas operations.
- Likely lower earnings in oil marketing, as COVID-19 significantly reduces demand for transportation.
- Tax rate at 20%-25%, cost of debt below 5%.
- Annual working capital outflow of THB10 billion.
- Capex of THB220 billion in 2020 and THB160 billion in 2021.
- Dividends of THB50 billion in 2020 and THB40 billion in 2021.

Based on these assumptions, we derive the following credit metrics:

- Reported EBITDA of THB250 billion in 2020 and THB280 billion in 2021.
- Discretionary cash flow of negative THB80 billion in 2020 and positive THB20 billion in 2021.
- Reported net debt of THB410 billion in 2020 and THB390 billion in 2021. Adjusted debt of THB600 billion in 2020 and THB580 billion in 2021.

- Adjusted debt-to-EBITDA ratio of 2.2x in 2020 and 2.0x in 2021.

Liquidity

PTT has adequate consolidated liquidity, meaning sources of funding will cover uses by 1.4x in 2020. In addition, sources of funds will exceed uses even if EBITDA declines by 15%.

We assess liquidity at the parent company to be adequate on account of its large cash balances, stable operating cash flows, dividends from subsidiaries and associates, and manageable debt maturities, despite prospective capex.

There are maintenance financial covenants on debt instruments at the subsidiaries' level (none at the parent or PTTEP), but we do not expect them to be a restriction, given the group's adequate headroom.

Principal liquidity sources include:

- Cash and cash equivalents of THB331 billion as of Dec. 31, 2019.
- Cash flow from operations before change in working capital of about THB200 billion over 2020.

Principal liquidity uses include:

- Short-term debt maturities of THB96 billion.
- Working capital investment of THB10 billion.
- Capital spending of THB220 billion.
- Dividend payments of about THB50 billion, including distributions to non-controlling interests.

Issue Ratings - Subordination Risk Analysis

Capital structure

PTT has two U.S. dollar-denominated notes--US$350 million (of which US$298 million is outstanding) maturing in 2035 and US$600 million (of which US$571 million is outstanding) coming due in 2042.

On Dec. 31, 2019, PTT had THB665 billion in debt, including PTTEP's perpetual securities (THB6 billion), which the company accounts for as equity. Of this, THB32 billion was secured debt (mainly at Thai Oil and PTTGC), and THB511 billion was unsecured debt at the subsidiaries' level. This means the ratio of priority debt (secured debt and debt at the operating subsidiaries level) to total debt was about 80%.

Analytical conclusions

We believe that companies with modest leverage present low subordination risks. Therefore, we equalize our issue ratings with the issuer credit rating on PTT. Increasing leverage at the group level could put pressure on the issue ratings.

Ratings Score Snapshot

Issuer Credit Rating

FC: BBB+/Stable/--; LC: A-/Negative/--

Business risk: Satisfactory

- Country risk: Moderately high
- Industry risk: Intermediate
- Competitive position: Satisfactory

Financial risk: Modest

- Cash flow/Leverage: Modest

Anchor: bbb+

Modifiers

- Diversification/Portfolio effect: Neutral (no impact)
- Capital structure: Neutral (no impact)
- Financial policy: Neutral (no impact)
- Liquidity: Adequate (no impact)
- Management and governance: Satisfactory (no impact)
- Comparable rating analysis: Neutral (no impact)

Stand-alone credit profile: bbb+

- Related government rating: FC: BBB+; LC: A-
- Likelihood of government support: Extremely high (no impact for FC rating; +1 notch from SACP for LC rating)

Related Criteria

- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments, April 1, 2019
- Criteria | Corporates | General: Reflecting Subordination Risk In Corporate Issue Ratings, March 28, 2018
- General Criteria: Guarantee Criteria, Oct. 21, 2016
- 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
- Criteria | Corporates | Industrials: Key Credit Factors For The Oil Refining And Marketing Industry, March 27, 2014

- Criteria | Corporates | Industrials: Key Credit Factors For The Midstream Energy Industry, Dec. 19, 2013
- Criteria | Corporates | General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Methodology: Timeliness Of Payments: Grace Periods, Guarantees, And Use Of 'D' And 'SD' Ratings, Oct. 24, 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
PTT Public Co. Ltd.		
Issuer Credit Rating		
Foreign Currency	BBB+/Stable/--	BBB+/Positive/--
Local Currency	A-/Negative/--	A-/Stable/--
Ratings Affirmed		
PTT Public Co. Ltd.		
PTT Treasury Center Co. Ltd.		
Senior Unsecured	BBB+	