

CHAROEN POKPHAND FOODS PLC

No. 21/2015

31 March 2015

Company Rating:	A+
Issue Ratings:	
Senior unsecured	A+
Outlook:	Stable

Company Rating History:

Date	Rating	Outlook/Alert
20/06/14	AA-	Negative
19/05/11	AA-	Stable
30/04/10	A+	Positive
22/06/06	A+	Stable
20/05/05	A	Positive
12/07/04	A	Stable
28/05/04	A	-
01/03/01	A+	-

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Rating Rationale

TRIS Rating lowers the company rating and existing issue ratings of Charoen Pokphand Foods PLC (CPF) to “A+” from “AA-”. The downgrade reflects weakening cash flow protection following major acquisition and longer-than-expected recovery of shrimp operation in Thailand. At the same time, TRIS Rating assigns the rating of “A+” to CPF’s proposed issue of up to Bt12,000 million in senior unsecured debentures. The proceeds from the new debentures will be used to repay CPF’s existing debts and used for planned capital expenditures.

The “A+” ratings continue to reflect the company’s leading position in the Thai agribusiness and food industry, its diverse range of products and markets, its efforts to create more branded food products, and its ample financial flexibility.

The inherent volatility of the prices for farm products, the exposure to disease outbreaks, the strengthening of Thai baht, and changes in regulations imposed by importing countries remain rating concerns.

CPF is the largest agribusiness and food conglomerate in Thailand. As of 13 March 2015, Charoen Pokphand Group Co., Ltd. (CPG) and related companies held 44.3% of CPF’s shares. CPF’s business is divided into two major categories, livestock and aquaculture. Each of these categories comprises feed, farm, and food products. Fully-integrated operations help CPF’s products meet safety and traceability standards, which qualify its products for export to major importing countries, including the countries of the European Union (EU), Asian nations, and the United States (US).

CPF’s revenue is geographically diverse. The operations in Thailand accounted for 41% of total revenue in 2014. China operations contributed 27% of total revenue, followed by 15% from operations in Vietnam. The remaining revenue came from Turkey, Taiwan, India, and other countries, which accounted for 1%-4% each. Animal feed, which is a relatively stable source of revenue, is the largest product segment, contributing about 53% of total revenue in 2014. Sales of commodity-like farm products contributed 35% of the company’s total sales in 2014 while revenue from the sales of food products accounted for 12%.

The company is striving to enlarge its portfolio of branded products and develop distribution channels for both the domestic and overseas markets. As of 31 December 2014, CPF’s distribution channels included 5,220 kiosks of Five-Star chicken, 201 Chester’s restaurants, 610 CP Fresh Mart shops, and about 15 stores under the CP Fresh Mart Plus, CP Kitchen, and CP Food World brands. CPF, through its subsidiary, C.P. Pokphand Co., Ltd. (CPP), operated in China and Vietnam, is building two food processing plants in China, one in Qinghuangdao and one in Qingdao.

In 2014, CPF’s operations improved from the low level of profit in 2013, thanks to the favorable prices for livestock in Thailand. CPF’s livestock price in overseas, especially Vietnam, was another factor underpinning the improved performance in 2014. However, the shrimp business in Thailand, one of the company’s major profit contributors, posted a loss for the second consecutive year, as the industry still struggles to recover from the Early Mortality Syndrome (EMS) problem. Operations in China, accounting for 27% of CPF’s revenues, had contended with an economic slowdown in China and higher operating expenses as the unit prepared for expansion. CPF’s total operating margin before depreciation and amortization improved to 5.6% in 2014, from a record low of 2.6% in 2013.

Earnings before interest, tax, depreciation, and amortization (EBITDA) increased by 83.6% to Bt31,438 million in 2014, compared with Bt17,124 million in 2013.

Despite the improved operating results in 2014, ongoing capital expenditures and aggressive expansion plans weakened CPF's balance sheet. After CPF completed major acquisition in 2012, CPF spent Bt20,000-Bt25,000 million each year for capital expenditures, plus Bt10,000 million for series of acquisitions and investments in 2013 and 2014, plus annual dividend payments of Bt6,000-Bt7,000. Consequently, total debt continued to climb, rising to Bt195,929 million in 2014 from Bt69,449 million in 2011. CPF's EBITDA improved at a slower pace than an increase in debt. This resulted in weaker cash flow protection. The EBITDA interest coverage ratio was 2.3-3.8 times in 2012-2014, compared with 3.3-11.8 times in 2007-2011. The fund from operation (FFO) to total debt ratio was 4.3%-9.3% in 2012-2014, compared with 11%-37% during 2007-2011.

In September 2014, CPF divested its 25% stake in CPP. CPF sold its holding to ITOCHU Corporation, one of the leading trading companies in Japan, for HK\$1.1 per share or Bt27,258 million in total. CPF's debt to capitalization ratio improved to 54.4% as of December 2014, from 59.0% in 2013 because the divestures boosted its equity base. CPP remains CPF's subsidiary, as CPF still holds 50.4% of total shares of CPP. Partnership with ITOCHU should help CPF further strengthen its distribution channels in many countries.

Looking forward, the slow recovery from the EMS plague may cause CPF's aquaculture business in Thailand to remain weak. The performance of the operation in China hinges on an economic recovery in China. CPF's livestock operations in Thailand, which recorded solid performances in 2014, will face more challenges in 2015. The stronger Thai baht against EURO and yen will hold back demand for export even though more countries have removed import bans for frozen chicken meat from Thailand. Domestic poultry prices in Thailand started to fall again after a major producer resumed and other producers expanded their production capacities. Swine prices plunged by nearly 20% during the first two months of 2015. These factors will make the livestock business in Thailand more volatile while the aquaculture unit will remain crippled. CPF continues to pursue its growth strategy. CPF has laid out plans for sizeable capital expenditures of about Bt28,000 million for 2015, excluding acquisitions. CPF recently announced it would buy an additional 75% stake in C.P. Cambodia Co., Ltd. (CPC). The total consideration for the transaction is Bt2,850 million. CPF still opts for acquisitions if the investment is aligned with CPF's core business and the acquired business generates a reasonable profit. The room for deleverage is limited, given its growth-driven strategy. The EBITDA interest coverage ratio and FFO to total debt ratio will take time to return to normal levels, given the slow recovery from the EMS outbreak and challenging environment in major operations.

CPF's liquidity and financial flexibility remain strong. As of 31 December 2014, CPF's had Bt39,320 million in cash on hand and short-term securities. The company owns 33.27% interest in CP All PLC (CPALL), the leading convenience store operator in Thailand. The market capitalization of CPALL was approximately Bt343 billion, as of 23 March 2015.

Rating Outlook

The "stable" outlook reflects TRIS Rating's expectation that CPF will maintain its leading position in the dynamic agribusiness and food industry. The company's diverse range of operations, products, and markets is expected to provide CPF some insulation from the cyclical nature of commodity-like farm products and disease epidemics. The rating upside will rely on the company's ability to manage its debt to capitalization to be 50%, and demonstrate significant improvement in debt serviceability on sustainable basis. In contrast, the ratings would likely be downgraded should any debt-funded acquisition materially deteriorate the balance sheet and further weaken cash flow protection.

Charoen Pokphand Foods PLC (CPF)

Company Rating:	A+
Issue Ratings:	
CPF15NA: Bt3,000 million senior unsecured debentures due 2015	A+
CPF163A: Bt6,060 million senior unsecured debentures due 2016	A+
CPF17NA: Bt5,000 million senior unsecured debentures due 2017	A+
CPF178A: Bt2,000 million senior unsecured debentures due 2017	A+
CPF185A: Bt6,000 million senior unsecured debentures due 2018	A+
CPF188A: Bt3,000 million senior unsecured debentures due 2018	A+
CPF198A: Bt6,000 million senior unsecured debentures due 2019	A+
CPF198B: Bt2,500 million senior unsecured debentures due 2019	A+
CPF218A: Bt3,000 million senior unsecured debentures due 2021	A+
CPF218B: Bt5,500 million senior unsecured debentures due 2021	A+

CPF228A: Bt4,000 million senior unsecured debentures due 2022	A+
CPF328A: Bt5,000 million senior unsecured debentures due 2032	A+
CPF418A: Bt4,000 million senior unsecured debentures due 2041	A+
CPF41DA: Bt6,000 million senior unsecured debentures due 2041	A+
Up to Bt12,000 million senior unsecured debentures due within 2023	A+
Rating Outlook:	Stable

Financial Statistics and Key Financial Ratios*

Unit: Bt million

	Year Ended 31 December				
	2014	2013	2012	2011	2010
Sales and service revenues	426,039	389,251	357,175	206,099	189,049
Gross interest expense	8,241	7,568	6,283	2,422	1,773
Net income from operations	5,914	(1,458)	3,930	14,476	11,592
Funds from operations (FFO)	18,269	8,027	9,486	17,480	17,455
Total capital expenditures	25,727	23,252	20,182	10,288	6,460
Total assets	416,764	365,003	310,544	160,506	126,092
Total debt	195,929	186,405	146,203	69,449	46,649
Shareholders' equity	163,966	129,573	120,781	67,077	60,944
Operating income before depreciation and amortization as % of sales	5.58	2.59	4.30	9.43	8.89
Pretax return on permanent capital (%)	6.35	2.94	7.49	16.32	15.63
Earnings before interest, tax, depreciation, and amortization (EBITDA) interest coverage (times)	3.81	2.26	3.58	10.18	11.76
FFO/total debt (%)	9.32	4.31	6.49	25.17	37.42
Total debt/capitalization (%)	54.44	58.99	54.76	50.87	43.36

* Consolidated financial statements

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