

31 MAY 2023

## Fitch Revises Outlook on HMC Polymers to Negative; Affirms at 'A-(tha)'

Fitch Ratings - Bangkok - 31 May 2023: Fitch Ratings (Thailand) Limited has revised the Outlook on HMC Polymers Company Limited, a polypropylene (PP) manufacturer, to Negative, from Stable. At the same time, Fitch has affirmed the National Long-Term Rating and senior unsecured rating at 'A-(tha)'.

The Negative Outlook reflects risks to improvement in operating cash flow over the next two years. We expect EBITDA to reach about THB3.5 billion by 2025 and for EBITDA net leverage to fall to about 3.0x. However, financial leverage could remain above 3.3x, the negative threshold for HMC's rating, if demand or margins do not recover as we expect or if the company's investments and shareholder returns exceed our forecasts, which could constrain deleveraging.

HMC's rating incorporates a one-notch uplift from its 'bbb+(tha)' Standalone Credit Profile (SCP), based on our assessment of moderate linkages with PTT Global Chemical Public Company Limited (PTTGC, AA(tha)/Stable, SCP: a+(tha)). PTTGC is HMC's largest shareholder, with a 41% stake.

HMC's SCP reflects its position as the largest PP producer in Thailand as well as its leading technology and product innovation, which enables it to focus on high-value-added products. However, this is balanced by limited product diversification, the cyclical petrochemical industry and our expectations of elevated near-term financial leverage.

### Key Rating Drivers

**Weak Profitability:** We expect EBITDA to remain weak, at about THB400 million, in 2023 with new PP capacity, mainly in Asia, pressuring product spreads. Energy prices are also likely to stay high, although lower than in 2022. However, EBITDA should be supported by higher sales volume since the start-up of PP Line 4 in December 2022 and reach THB1.9 billion in 2024 amid better product spreads, with PP spreads at mid-cycle levels in 2025-2026.

HMC reported negative EBITDA in 2022, at negative THB149 million, amid narrow product spreads, with PP/propylene spreads hitting historical lows as a result of softer demand and higher feedstock costs. Moreover, higher increase in propane costs eroded HMC's margin. We expect the volatility in PP spreads to continue in 2023, with only a modest improvement from 2022.

**Risk to Deleveraging:** We expect EBITDA net leverage to remain above 3.3x in 2023-2024, due to weak EBITDA and rising net debt, as we forecast negative cash flow from operations in 2023. However, net debt should decrease in 2024-2025 and net leverage fall to about 3.0x by 2025, once EBITDA recovers in 2024-2025 and reach THB3.5 billion in 2025. We do not expect any dividend payments until 2026,

when the company is likely to make a net profit.

**Lower Capex:** Capex is likely to fall, as HMC does not have any large capex plans after it completed its PP Line 4. It has budgeted capex of THB3.1 billion for 2023-2025, mainly for maintenance of all facilities and major maintenance of its propane dehydrogenation plant.

**Focus on High-Value-Added Products:** HMC focuses on differentiated and specialty products, which have lower competition and higher margins. The proportion of sales from these products increased to 50%-55% in 2020-2022, from about 35% in 2015, although we expect this to drop in 2023 during PP Line 4's ramp-up. The company aims to raise the contribution to about 70% of sales by 2030. HMC said the products provide a premium of about 5% over its commodity PP product price, which supports higher profitability than its competitors.

**Leading South-East Asian PP Producer:** HMC is the largest PP producer in Thailand, with about a one-third market share. HMC's capacity increased to about 1.1 million tonnes per annum by end-2022, which also makes it the largest PP producer in south-east Asia. Its market position is enhanced by its focus on differentiated and specialty products, and partial upstream integration into a propane dehydrogenation plant.

**Leading Technology, Product Innovation:** HMC uses leading PP technology from LyondellBasell Industries N.V. (BBB/Positive), a key shareholder, in its production. It uses the latest technology for its PP Line 4 - one of only two plants in the world that can use hexene co-monomer to enhance PP properties - and to expand its product portfolio for new applications. HMC is the leader in pipe- and medical-grade PP in Thailand, and is the world's first producer of PP for dielectric film using modern technology. All of HMC's products use LyondellBasell's global brands.

**Cyclicity and Limited Diversification:** HMC's credit profile is tempered by its limited product diversification and the inherent cyclicity of the industry. Its earnings and cash flow are subject to volatile petrochemical prices and margins as well as demand-supply dynamics. HMC also produces only PP products, making it less diversified than domestic chemical peers.

**Linkage with PTTGC:** We assess that the parent, PTTGC, has a 'Medium' incentive to support HMC under our Parent and Subsidiary Linkage Rating Criteria. HMC is a propylene off-taker of PTTGC, and its key vehicle in the PP business. HMC has a non-compete arrangement with PTTGC for petrochemical products, reflecting the strategic linkages. We believe PTTGC is likely to provide extraordinary support to HMC, if needed. This underpins our assessment of 'Medium' strategic incentives for the parent to provide support.

PTTGC does not have management control over HMC, as LyondellBasell is also involved in the appointment of HMC's directors and key senior management. In addition, all of HMC's products use LyondellBasell's global brand names. We therefore assess the operational incentive as 'Weak', the same as the legal incentive.

## Derivation Summary

HMC's business profile is moderate relative to that of Thai downstream oil and gas, and chemical peers. Its financial profile is also moderate during the normal run of business.

HMC has a smaller operating scale as well as lower upstream integration and product diversification than IRPC Public Company Limited (A-(tha)/Negative, SCP: bbb(tha)). However, HMC is more advanced in product and technology, and generates higher margins, even excluding the refinery business, due to its focus on differentiated and specialty products. This, together with our expectations of stronger credit metrics - in line with historical trend - results in HMC's SCP being one notch higher than that of IRPC. Both companies face the risks associated with high leverage over the next year or two, as reflected in the Negative Outlook on their ratings.

HMC's business profile is slightly stronger than that of other companies in the polymer and plastic-product business, including Polyplex (Thailand) Public Company Limited (PTL, A-(tha)/Stable) and Eastern Polymer Group Public Company Limited (EPG, A-(tha)/Stable). We believe HMC's leading market position in south-east Asia offsets its lower geographical diversification compared with PTL, and its fewer end-user segments compared with EPG. Still, HMC's financial leverage leads to a lower SCP than at the two peers.

## **Key Assumptions**

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

- Sales volume to increase by about 28% in 2023 (2022: 6%) following the start-up of PP Line 4 in December 2022, and by 2%-4% in 2024-2025.
- Flat PP/propylene spreads in 2023, gradually improving in 2024-2025.
- Capex of THB3.1 billion in total over 2023-2025.
- No dividend payment until 2026, using 2025 net profit.

## **RATING SENSITIVITIES**

Factors that could, individually or collectively, lead to positive rating action/upgrade:

- The Outlook could be revised to Stable if HMC is on track to reduce EBITDA net leverage to below 3.3x by 2025, while PTTGC's incentive to provide support remains unchanged.

Factors that could, individually or collectively, lead to negative rating action/downgrade:

- Weaker operating cash flow than we expect, increasing debt-funded investments or dividend payouts, resulting in EBITDA net leverage remaining above 3.3x for a sustained period.
- Weakened ties with PTTGC.

## **Liquidity and Debt Structure**

**Manageable Liquidity:** HMC had outstanding debt of THB14.2 billion at end-2022, consisting of THB1.1 billion in short-term loans, THB5.0 billion in debentures and THB8.1 billion in long-term bank loans. Debt maturing during 2023 of THB2.6 billion, including short-term loans, and expected negative free cash flow will be supported by cash on hand of THB1.4 billion and committed, available revolving credit facilities of THB7.5 billion. HMC received the committed revolving credit facilities from two domestic banks in January and May 2023, with three- and five-year terms.

## **Issuer Profile**

HMC is the first and largest PP manufacturer in Thailand. The company operates four lines of PP with a total capacity of 1.06 million tonnes per annum. PP Line 4 started commercial operation in December 2022. Its products are sold under LyondellBasell brand names.

## **Summary of Financial Adjustments**

Preferred shares, which are proportionately held by shareholders, are excluded from debt.

## **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.

## **Public Ratings with Credit Linkage to other ratings**

HMC's rating receives a one-notch uplift based on our assessment of 'Medium' incentives for support from the parent, PTTGC.

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**Rating Actions**

ENTITY/DEBT	RATING		RECOVERY	PRIOR
HMC Polymers 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 \(pub.22 Dec 2020\)](#)

[Parent and Subsidiary Linkage Rating Criteria \(pub.01 Dec 2021\)](#)

[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)

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