20 May 2020 | Affirmation

Fitch Affirms Chandra Asri at 'BB-'; Outlook Stable

Fitch Ratings-Singapore-20 May 2020:

Fitch Ratings has affirmed PT Chandra Asri Petrochemical Tbk's (CAP) Long-Term Issuer Default Rating (IDR) at 'BB-'. The Outlook is Stable. The agency also affirmed CAP's senior unsecured US dollar bond at 'BB-'.

CAP's ratings reflect its moderate linkages with its dominant 46% shareholder, PT Barito Pacific Tbk (B+/Stable). Consequently, Fitch rates CAP based on the consolidated credit profile of Barito, based on our Parent and Subsidiary Rating Linkage criteria. We expect Barito's consolidated financial profile to weaken in 2020 with consolidated funds from operations (FFO) net leverage rising to around 4.2x (2019: 3.1x) on weaker CAP earnings due to lower petchem price and volume assumptions. However, the profile should improve as we expect net leverage in 2021 to come down to 3.1x - below Fitch's negative rating trigger of 4.0x - as CAP's earnings improve.

We continue to assess CAP's Standalone Credit Profile (SCP) at 'bb-', reflecting its leading market position, integrated operation, diverse product offering and strong financial profile. The SCP is constrained by CAP's asset-concentration risk and limited operating scale, compared with global chemical peers, and the cyclical nature of the petrochemical industry. CAP also has financial flexibility on capex for its second petrochemical complex (CAP2) project. We expect a final investment decision (FID) on the CAP2 project to be taken in early to mid-2021 - we previously expected end-2020.

Key Rating Drivers

Leading Market Position; Integrated Operations: CAP's SCP benefits from its leading market position as Indonesia's largest petrochemical producer, accounting for about 35% of the country's olefin and polymer production capacity. Its market position is also aided by better-integrated operations than those of domestic peers as well as a diverse product offering and customer base. This, together with its plant being located close to key customers with pipeline connectivity to some, will continue to support higher realisations and profitability.

Pressure on Spreads: Average product spreads fell in 2019, resulting in CAP's EBITDA margin falling to 9.3% from 15.6% in 2018. We expect spreads to stay low for most petrochemical products affected by demand reduction amid the coronavirus pandemic, as well as supply concerns from global capacity additions. We expect a marginal improvement in CAP's EBITDA margin to 10.6% in 2020, mainly as a result of an increase in the proportion of higher-margin polyolefins in the sales mix. We expect CAP to face less pressure than domestic peers due to flexibility in varying its products, diversified suppliers and long-term customer relationships. Its association with 31% shareholder SCG Chemicals Company Limited also helps its feedstock procurement.

Temporary Decline in Volumes: Fitch expects the muted demand environment in 2020 to affect the full utilisation of CAP's enhanced capacities. We cut our forecast for CAP's total sales volumes to 2,468 kilotonnes (kt) from 2,737kt previously. The company has not had any material plant shutdown in the year to date and has not reduced its utilisation levels. CAP is exempt from the Indonesian government's large-scale social-distancing measures in response to the coronavirus due to its status as a vital national object. In addition, the impact of lower demand in the event of a protracted economic downturn is likely to hit imports first, as Indonesia imports more than 50% of its petrochemical product requirements.

Moderate Linkages with Parent: Fitch rates CAP on the consolidated credit profile of Barito group, which benefits from a diversified presence across the petrochemical and energy businesses. In addition to 46% stake in CAP, Barito owns about 35% to 40% of the operating assets of Star Energy Group Holdings Pte Ltd., which has established operations and long-term contracts with state power utility PT Perusahaan Listrik Negara (Persero) (PLN, BBB/Stable), resulting in stable revenue and cash flow. Star Energy's inherently low operating costs, long operating history and cash flow visibility enhance Barito's consolidated credit profile.

Modest Consolidated Profile: We expect CAP's lower EBITDA generation to affect Barito's consolidated financial profile, with consolidated FFO net leverage rising to around 4.2x in 2020. However, the profile should improve in 2021, as CAP's sale volumes increase along with marginal improvement in petrochemical product spreads. We expect CAP's financial profile to stay strong, with FFO adjusted net leverage below 1.5x over the next two to three years after weakening to 1.7x in 2020 (2019: 0.8x).

Flexible Capex: CAP planned to invest about USD330 million in 2020 on CAP2, out of a total USD430 million capex budget. However, CAP expects to delay the final investment decision (FID) for CAP2 to 2021. This will push back much of the investment for the project. We estimate total investment costs for CAP2 to be around USD5 billion, but have only factored in pre-FID capex - mainly land-acquisition costs - in our analysis, as the project's ownership and funding structure are yet to be finalised.

Barito also has a modest investment plan for its power business via a medium- to long-term expansion of Star Energy's geothermal operation. In addition, Barito plans to invest in a 2GW greenfield Indonesian coal-fired power project - PT Indo Raya Tenaga - in which Barito has a 49% stake. Fitch only factors in the equity outflow from Barito in its cash flow forecast due to the probable non-recourse nature of the project-finance debt usually taken on such projects.

Derivation Summary

CAP's ratings reflects Barito group's diversified business across the petrochemical and energy businesses, its leading market position as Indonesia's largest petrochemical producer, integrated operation and a strong record of geothermal operation with long-term contracts driving stable revenue. The ratings also reflect Barito group's moderate consolidated financial profile. CAP's stronger standalone financial profile counteracts the group's weaker financial profile, resulting in a similar assessment of the two entities' credit profiles.

Ineos Group Holdings S.A. (BB+/Stable) is the world's largest commodity chemical producer, with diversified integrated production facilities, access to low-cost feedstock and feedstock flexibility. CAP's smaller scale and limited geographical diversification results in its rating being lower by two notches, despite a stronger financial profile.

PJSC Kazanorgsintez (B+/Stable) is one of Russia's largest chemical companies and the country's largest polyethylene producer. We believe CAP's more diversified product profile and larger size justifies the one-notch difference in the two entities' ratings, despite similar financial profiles. Barito group's weaker financial profile and fractured shareholding counteracts its access to diversified cash flow compared with that of PJSC Kazanorgsintez, resulting in a similar rating assessment of the two entities.

Key Assumptions

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

- Product spreads of key petrochemical products to weaken modestly in 2020 and improve gradually there-after

- Gradual increase in utilisation of enhanced polyethylene and polypropylene capacities

- CAP capex of around USD200 million in 2020, including around USD90 million pre-FID capex on CAP2; the pre-FID capex balance to be pushed to 2021 and 2022

- CAP dividend payout ratio of 40%

- Consolidated Barito group capex of around USD850 million over the next three years

- Star Energy's units operating at an average availability rate of around 94% and their tariffs in line with PLN's long-term contracts

RATING SENSITIVITIES

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

Positive rating action is not probable in the near-to-medium term pending the FID and funding structure for CAP2. An upgrade in CAP's rating would only result from an improved SCP combined with a similar improvement in Barito group's credit profile. However, we do not expect this to occur in the near-to-medium term due to CAP's limited scale and diversification and potentially high uncommitted capex. CAP's SCP could be raised upon a significant improvement in its business profile, as seen by larger scale and vertical linkages that increase business diversification, while maintaining a strong financial profile, such that FFO net leverage does not exceed 1.5x on a sustained basis.

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

Deterioration in Barito group's consolidated credit profile, with FFO net leverage exceeding 4.0x for a sustained period, which may arise from large, debt-funded capex on CAP2.

For CAP's SCP, deterioration of its financial profile resulting in FFO net leverage exceeding 3.0x for a sustained period.

Best/Worst Case Rating Scenario

International scale credit ratings of Non-Financial Corporate issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of four notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit https://www.fitchratings.com/site/re/10111579.

Liquidity and Debt Structure

Strong Liquidity: CAP has strong liquidity, with a cash balance of USD668 million and undrawn committed credit facilities of about USD181 million as of end-2019, against a total debt balance of USD804 million and scheduled debt maturities of USD68 million in 2020. CAPS's debt maturity schedule is well spread out, with annual debt maturities not exceeding USD130 million until 2024, when its USD300 million notes are due. CAP also has strong relationships with domestic banks and has access to some Thai banks due to its linkages with the Siam Cement group, one of Thailand's largest conglomerates.

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.

ESG Considerations
The highest level of ESG credit relevance, if present, is a score of 3. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity(ies), either due to their nature or to the way in which they are being managed by the entity(ies). For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg.

PT Chandra Asri Petrochemical Tbk; Long Term Issuer Default Rating; Affirmed; BB-; RO:Sta
----senior unsecured; Long Term Rating; Affirmed; BB-

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Additional information is available on www.fitchratings.com

Applicable Criteria

Corporate Rating Criteria (pub. 01 May 2020) (including rating assumption sensitivity)
Corporates Notching and Recovery Ratings Criteria (pub. 14 Oct 2019) (including rating assumption sensitivity)
Country-Specific Treatment of Recovery Ratings Rating Criteria (pub. 27 Feb 2020)
Parent and Subsidiary Rating Linkage (pub. 27 Sep 2019)
Sector Navigators: Addendum to the Corporate Rating Criteria (pub. 01 May 2020)

Applicable Model

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).
Corporate Monitoring & Forecasting Model (COMFORT Model), v7.9.0 (1)

Additional Disclosures

Dodd-Frank Rating Information Disclosure Form
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