PEFINDO
CREDIT RATING AGENCY

Rating Rationale

PT Perkebunan Nusantara X

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CREDIT PROFILE

Corporate Rating	*$_{id}$BBB+/Stable*
Rated Issues	
MTN 2018	*$_{id}$BBB+*
Rating Period	
August 13, 2020 – February 1, 2021	
Rating History	
FEB 2020	*$_{id}$BBB+/Stable*
FEB 2019	*$_{id}$BBB/Stable*
FEB 2018	*$_{id}$BBB/Stable*
FEB 2017	*$_{id}$BBB/Stable*
APR 2016	*$_{id}$BBB+/Stable*
APR 2015	*$_{id}$BBB+/Stable*
DEC 2014	*$_{id}$BBB+/Negative*
AUG 2014	*$_{id}$A/Negative*
APR 2014	*$_{id}$A+/Stable*
APR 2013	*$_{id}$A+/Stable*

FINANCIAL HIGHLIGHTS

As of/for the year ended	**Jun-2020** (Unaudited)	**Dec-2019** (Audited)	**Dec-2018** (Audited)	**Dec-2017** (Audited)
Total adjusted assets [in IDR Bn]	12,406.0	12,142.7	12,418.4	11,083.2
Total adjusted debt [in IDR Bn]	1,948.8	1,992.4	2,279.4	2,346.7
Total adjusted equity [in IDR Bn]	8,505.6	8,563.1	8,405.9	6,997.3
Total adjusted sales [in IDR Bn]	776.8	2,619.1	2,597.5	2,562.8
EBITDA [in IDR Bn]	54.3	529.9	536.7	422.1
Net income after MI [in IDR Bn]	(65.4)	107.9	104.8	52.3
EBITDA margin [%]	7.0	20.2	20.7	16.5
Adjusted debt to EBITDA [X]	*17.9	3.8	4.2	5.6
Adjusted debt to adjusted equity [X]	0.2	0.2	0.3	0.3
FFO to adjusted debt [%]	*(4.2)	13.4	12.2	6.5
EBITDA to IFCCI [X]	0.6	2.4	2.2	1.8
USD Exchange Rate in IDR	14,302	13,901	14,481	13,548

FFO = EBITDA – IFCCI + Interest Income – Current Tax Expense
EBITDA = Operating Profit + Depreciation Expense + Amortization Expense
IFCCI = Gross Interest Expense + Other Financial Charges + Capitalized Interest; (FX Loss not included)
MI= Minority Interest *annualized

The above ratios have been computed based on information from the company and published accounts. Where applicable, some items have been reclassified according to PEFINDO's definitions.

Ratings for PT Perkebunan Nusantara X and its MTN affirmed at "$_{id}$BBB+" with stable outlook

PEFINDO has affirmed its **"$_{id}$BBB+"** ratings for PT Perkebunan Nusantara X (PPNX) and its Medium-Term Notes (MTN) Year 2018. The outlook for the corporate rating is **"stable"**.

An obligor rated $_{id}$BBB has an adequate capacity to meet its long-term financial commitments relative to that of other Indonesian obligors. However, adverse economic conditions or changing circumstances are more likely to weaken its capacity to meet its financial commitments. The plus (+) sign indicates that the rating is relatively strong within its category.

The rating reflects its position as one of the largest sugar producers in Indonesia with good productivity, its vertically-integrated operations with more product diversity expected, and stable domestic demand for sugar. The rating is constrained by the Company's moderate financial profile, high dependency on farmers' sugar cane supply, and exposure to the fluctuations of product prices and unfavorable weather.

We may raise the rating if PPNX's credit profile continues to improve on a sustained basis as a result of deleveraging plans through assets disposal initiatives and/or if the Company's achievement is better than projection. However, the rating may be lowered if the Company incurs greater debt than projected and/or its financial profile deteriorates due to weaker-than-expected cash flow and/or profitability, stemming from a major slowdown in its core businesses – sugar, edamame, and tobacco – and a decline in commodity prices. We are aware that the Company is in the middle of restructuring its bank loans as a part of its parent long term financial transformation plan. However, PEFINDO doesn't incorporate yet the long term financial transformation plan on its parent in the rating scenario as it is still in the process.

The divestiture of its subsidiary, PT Nusantara Medika Utama, will result in a thinner revenue cushion for the Company during the low price of commodities, in our view. However, it is mitigated by a proceed of around IDR80 billion (after-tax) that can be used to deleverage its debt position. Besides, the Coronavirus Disease (COVID-19) pandemic also caused an increase in domestic sugar prices that, to some extent, benefited the Company as a result of the lockdown policies implemented by exporting countries. This policy makes it difficult for the sugar import process to stabilize the gap between supply and demand at domestic. Factoring those conditions, we are of the view that PPNX's overall credit profile is still commensurate with the current **"$_{id}$BBB+"** rating.

Located in East Java, PPNX is a vertically-integrated plantation company engaged in the short-lived crops industries (sugar, edamame, and tobacco) and also producing downstream products through bio-ethanol plant. It processes sugar cane in its nine sugar cane mills with some of the by-product, molasses, as a feedstock to its bio-ethanol plant. At the end of 2019, it managed a total plantation area of 51,840 hectares (ha) of sugar cane plantations (including those owned by farmers), 1,351 ha of edamame plantations, and 511 ha of tobacco plantations. As of June 30, 2020, it was 90.0% owned by PT Perkebunan Nusantara III (Persero) (PTPN, $_{id}$BBB/Creditwatch Negative) and 10.0% by the Indonesian government.

Supporting factors for the above rating are:

- ***One of the largest sugar producers in Indonesia with good productivity.*** PEFINDO views the Company as one of the largest sugar producers in Indonesia, accounting for around 5% of total domestic production. In terms of domestic sugar supply, it has a market share of around 1-2%, given the country's reliance on imported sugar. We expect its share of domestic sugar supply to be maintained in this range over the near to medium term on the back of our expectation that Indonesia will continue to import sugar to meet local demand and stabilize prices. The Company also has good productivity, with an average sugar production yield of 5.9 tons/ha during the last three years (2017-2019). This is higher than the national average yield of 5.2 tons/ha in the same period. This good productivity is due to the Company's efforts to find better plantation areas that produce quality sugar cane and its better milling time-management.

- ***Vertically-integrated operations with more product diversity expected.*** PPNX has vertically-integrated operations, from spanning, planting, cultivating, harvesting, to processing sugar cane. Its sugar cane plantations are supported by nine sugar mills with a total capacity of 38,650 tons of cane per day (TCD), which will increase to 39,450 TCD in 2020 after the revitalization and capacity expansion of its Gempolkrep sugar mill are completed. This revitalization will increase the sugar mill's production capacity to 8,000 TCD from 6,500 TCD, and will add facilities to produce refined sugar, which will expand its market to include the industrial segment. We are of the view that its vertically-integrated operations and more diversified products will ensure revenue sustainability, leading to better operational efficiency and offsetting the risk of a demand drop-off from any particular product.
- ***Stable domestic demand for sugar.*** We are of the view that domestic demand for sugar will remain strong, as it is one of the nine basic foods for the public. The total domestic demand for sugar has stood at an average of 3.1 million tons per year during the last three years, mostly from households. Domestic producers have only been able to supply around 70% of this domestic demand, resulting in the need to import to fill in the gap. On top of that, Indonesia's large and growing population also creates potential additional domestic demand.

Constraining factors for the above rating are:

- ***Moderate financial profile.*** Although PPNX's financial profile has been improving over the past few years, we are of the view that it will remain at a moderate level in the near to medium term as its deleveraging process is heavily dependent on asset disposal initiatives, which have high uncertainty due to the market conditions, especially amid the pandemic. It also needs an annual capital expenditure of around IDR200-300 billion to maintain its production facilities. Factoring in these conditions, we expect its debt to EBITDA ratio to hover around 4.8x and interest coverage of around 1.9x in the near to medium term.
- ***High dependency on farmers' sugar cane supply.*** We are of the view that the Company has a high dependency on farmers, as more than 90% of its sugar cane needs are still procured from them. In the near to medium term, we are of the view that this condition will continue and could pose a risk to its cash flow if the farmers' sugar cane areas shrink. This occurred in 2017 when the farmers switched to planting other commodities, leading to a decline in the Company's sugar cane production volume. This occurred again in 2019 when the Company's sugar cane procurement mechanism was less favorable than its competitors.
- ***Exposure to the fluctuations of product prices and unfavorable weather.*** PPNX's business performance is significantly exposed to the fluctuations of sugar prices, as this commodity generates most of its cash flow. We note that the domestic price of sugar is relatively volatile despite the benchmark price set by the government, and any significant sugar price deterioration, as occurred in 2014, will have a significant negative impact on its cash flow. Business performance is also moderately exposed to adverse weather conditions, such as a prolonged dry season or an intense rainy season, which could affect production volume. A significant pest attack on its plantations, especially on its edamame plantations, could also negatively impact its business performance.