FitchRatings

RATING ACTION COMMENTARY

Fitch Affirms Pelindo at 'BBB' with Stable Outlook; Rating Watch Resolved

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Fitch Ratings - Jakarta - 14 Dec 2021: Fitch Ratings has affirmed Indonesia-based port operator PT Pelabuhan Indonesia (Persero)'s (Pelindo) Long-Term Foreign-Currency Issuer Default Rating (IDR) at 'BBB'. The Outlook is Stable. The Rating Watch Negative has been resolved.

Fitch has also upgraded Pelindo's USD500 million senior unsecured bond due 2023 and USD500 million senior unsecured bond due 2024 to 'BBB' from 'BBB-'. The Rating Watch Positive on these bonds has been resolved.

RATING RATIONALE

The affirmation follows the merger of four Indonesian state-owned port operators in October 2021, with PT Pelabuhan Indonesia II (Persero) as the surviving entity. The merged entity was renamed Pelindo. The affirmation also follows the acquisition by its subsidiary of a 55% stake it did not hold in a toll road asset. Pelindo's 'BBB' ratings are equalised with that of the Indonesian sovereign (BBB/Stable). It reflects strengthening of linkages with the Indonesian sovereign and a downward revision in its standalone credit profile (SCP) to 'bbb-' from 'bbb'.

Pelindo's strengthening linkages with the Indonesia sovereign, as assessed under our Government-Related Entities Rating Criteria, reflects its role and position as the sole state-owned port entity following the merger. It also reflects stronger government control over the important logistics supply chain for the country and the higher socio-political implications of a default by Pelindo, given its dominance in Indonesia's cargo transport and inter-island connectivity.

Pelindo's SCP of bbb-' reflects a high consolidated leverage profile, mainly driven by its recent acquisition of the toll road, which will carry debt of IDR7 trillion-9 trillion, and its consolidated capex plan of nearly IDR45 trillion over 2021-2025. The 34 km toll road, which connects Cibitung in Bekasi and Cilincing in North Jakarta, may reduce congestion at Tanjung Priok port and link areas with strategic industries to Tanjung Priok port. Pelindo expects the toll road to be in full operation by end of 2022.

The SCP is supported by Pelindo's dominance of the container port industry in Indonesia, strategic location of its flagship ports as well as the long term of its concession, which ensures visibility of group cash-flow generation. Pelindo's net debt/adjusted EBITDA is forecast to average 6.5x over 2021-2025 in our rating case. EBITDA is adjusted to account for dividend income from associates.

KEY RATING DRIVERS

Stronger Linkages with Sovereign:

Fitch has revised Pelindo's status, ownership and control by the sovereign to 'Very Strong' from 'Strong' following the merger of the four state-owned port operators. The state fully owns Pelindo and appoints its commissioners and board. It also controls its investment plans and capex decisions. We assess the record of state support to Pelindo as 'Strong'. There is limited record of the government providing tangible support to Pelindo, as it had a sound financial profile. However, we expect the company to receive government support, if needed, due to its important role in the country's economic development. Pelindo received a IDR1.2 trillion capital injection to develop Bali Maritime Tourism Hub in Benoa, Bali.

State's Incentive to Support Strengthened:

Fitch has revised Pelindo's socio-political implications of default to 'Strong' from 'Moderate'. We believe that a default would damage the government's reputation and substitution may be difficult as Pelindo is largest and sole state-owned company in the sector. Our assessment of the financial implications of a default by Pelindo is 'Strong', as the company is regarded as one of Indonesia's key state-owned entities and a default would hamper investor confidence in the sovereign and other state-owned entities.

Market Leading Port Operator: Revenue Risk: Volume - Stronger

Pelindo is the only Indonesian state-owned port operator, operating the primary ports of call across the country. It has 87 ports across the archipelago, including four of the country's flagship ports. Pelindo dominates Indonesia's container market and faces limited competition. Its traffic is mainly origin and destination (O&D) with limited transhipment cargo. The concessions for most of its ports have 50-year terms, ending in 2065. Land access to Pelindo's ports is largely via road with limited rail links. Tanjung Priok, with a draft of 16 metres, can handle vessels of 12,000 twenty-foot equivalent units.

Moderate Pricing Flexibility Supported by Fixed Rental Income: Revenue Risk: Price - Midrange

Pelindo has entered into a landlord business model with its JV partners, which provides unregulated and stable cash flow of around 9% of total revenue and 27% of EBITDA. Pelindo's tariffs are commercially negotiated with shipping associations but require consultation with the Ministry of Transport. This limits the company's pricing flexibility, as demonstrated by flat tariffs for its international containers over the past few years. However, tariffs on domestic containers have been increasing. The tariff structure, once fixed, will remain valid for at least two years.

Significant but Manageable Planned Capex: Infrastructure Development/Renewal - Midrange

The container capacity at Pelindo's major port, Tanjung Priok, is well-utilised, despite capacity additions across its major ports. Pelindo is building the Kalibaru terminal to add capacity in Tanjung Priok. The company is also developing the Kijing Port, Kuala Tanjung Industrial Estate and a new port in Makassar to support the economic growth of Kalimantan, Sumatera and Sulawesi, respectively. In addition, Pelindo is supporting the government tourism programme by developing Bali Maritime Tourism Hub in Benoa, Bali and has received capital injections from the state for this project. The company recently acquired the Cibitung-Cilincing toll road to reduce congestion and provide connectivity between Tanjung Priok port and industrial areas.

Most of its major projects are national strategic projects under a presidential decree. Management expect to incur total capex of nearly IDR45 trillion over 2021-2025. We expect Pelindo to raise debt to finance the capex, but we believe management's extensive experience in building and investing in ports mitigate the infrastructure development and renewal risk.

Heavy Use of US-Dollar Fixed-Rate Bullet Notes: Debt Structure - Midrange

Pelindo's consolidated debt comprises mainly senior unsecured bonds denominated in US dollars with bullet payment structures. This presents significant refinancing risk to the company, although this is mitigated by Pelindo's established access to capital markets. Pelindo has limited exposure to floating interest rates, given its fixed-rate bonds. However, the debt structure assessment is constrained by the lack of covenants and reserve accounts for its debt. Pelindo does not enter into any hedging transactions and relies on natural hedging from its US-dollar revenue.

PEER GROUP

Lonsdale Finance Pty Ltd (BBB/Stable) is the issuing entity for the Port of Melbourne, one of the largest container ports in Australia by throughput. Pelindo and Port of Melbourne have similar assessments for volume risk, reflecting their positions as primary ports, their diverse cargo types and customers, and their strong O&D traffic with limited transhipment. Port of Melbourne has a stronger price-risk assessment, underpinned by a long-term lease agreement, which provides stable cash flow of around one-third of total revenue, while Pelindo has a fixed rental income that contributes about 9% of its consolidated revenue. Port of Melbourne also has stronger infrastructure development risk as its future capex requirement is limited.

Both companies have similar debt structure assessments, as they issue corporate-like debt. Port of Melbourne has a five-year average leverage of 8.5x with a maximum of 9.2x. Port of Melbourne's significant long-term lease and limited capex counterbalance its higher leverage, resulting in a better credit assessment.

DP World Limited (DPW, BBB-/Stable) is the fifth-largest container port operator globally with a gross volume market share of around 9% and long average concession life. DPW benefits from a global network of port concessions focused on key east-west trade routes and faster growing markets. Meanwhile, Pelindo is the largest port operator in Indonesia with dominance of the container market. DPW has a five-year average leverage of 5.8x with maximum of 6.1x. Pelindo's comparable business and financial profiles justify a similar credit assessment, in our view.

RATING SENSITIVITIES

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

- Downgrade of Indonesia's sovereign rating

- Material weakening of linkages with sovereign

- Pelindo's SCP may be revised down if the Fitch-adjusted net debt/EBITDA is sustained above 7.0x under Fitch's rating case.

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

- Upgrade of Indonesia's sovereign rating provided linkages remain intact.

- Pelindo's SCP could be revised up if there is sustained improvement in its Fitch-adjusted net debt/EBITDA to below 6.0x under Fitch's rating case.

BEST/WORST CASE RATING SCENARIO

International scale credit ratings of Sovereigns, Public Finance and Infrastructure 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 three 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.

CREDIT UPDATE

On 1 October 2021, PT Pelabuhan Indonesia I (Persero), PT Pelabuhan Indonesia III (Persero) and PT Pelabuhan Indonesia IV (Persero) merged with Pelindo II. Pelindo II was the surviving entity after the merger, and was renamed Pelindo. The assets and liabilities of the other three operators were transferred to the surviving company, including outstanding senior unsecured dollar bonds. All four port operators are fully owned by the government of Indonesia. Hence, their ultimate ownership remains the same and the merger did not trigger a change-of-control event.

Pelindo's consolidated container throughput fell by 7% to 15.5 million twenty-foot equivalent units in 2020 due to the effects of the Covid-19 pandemic. In comparison, Indonesia's GDP contracted by 2.1% in 2020.

In addition, Pelindo recently acquired through a subsidiary a 55% stake in PT Cibitung-Tanjung Priok Tollways (CTP), a project company for a 34 km toll road connecting Cibitung in Bekasi and Cilincing in North Jakarta. With the acquisition, Pelindo now owns 100% of the toll road. The road is currently under construction and management expects to achieve full commercial operation by 2022.

FINANCIAL ANALYSIS

The Fitch base case forecasts container throughput to recover to the pre-pandemic level in 2022, in line with management's guidance. We forecast throughput to increase in line with the average GDP multiplier of 0.8x thereafter. We assume EBITDA margin will average 34% and capex will total IDR45 trillion over 2021-2025. Pelindo's leverage is mainly driven by the acquisition of the toll road asset. Fitch's base case generates an average adjusted net debt/EBITDA of 4.8x over 2021-2025, with a maximum of 5.4x in 2022.

The Fitch rating case assumes container throughput recovery in 2023 and an increase in line with the average GDP multiplier of 0.8x thereafter, reflecting our current assessment of the impact of the Covid-19 pandemic on throughput growth. We assume EBITDA margin will average at 28% and total capex will be similar to the Fitch base case over 2021-2025. The Fitch rating case generates an average adjusted net debt/EBITDA of 6.5x over 2021-2025, with a maximum of 7.1x in 2022.

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

Pelindo's rating is credit linked to that of the Indonesian sovereign.

ESG CONSIDERATIONS

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

RATING ACTIONS

ENTITY / DEBT	RATING			PRIOR
PT Pelabuhan Indonesia (Persero)	LT IDR	BBB Rating Outlook Stable	Affirmed	BBB Rating Watch Negative
PT Pelabuhan Indonesia (Persero)/Senior Unsecured/1 LT	LT	BBB Rating Outlook Stable	Affirmed	BBB Rating Watch Negative
PT Pelabuhan Indonesia (Persero)/Senior Unsecured/2 LT	LT	BBB Rating Outlook Stable	Upgrade	BBB- Rating Watch Positive

VIEW ADDITIONAL RATING DETAILS

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APPLICABLE CRITERIA

Government-Related Entities Rating Criteria (pub. 30 Sep 2020)

Ports Rating Criteria (pub. 16 Oct 2020) (including rating assumption sensitivity)

Infrastructure and Project Finance Rating Criteria (pub. 24 Aug 2021) (including rating assumption sensitivity)

APPLICABLE MODELS

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

GIG InForM Model, v1.0.0 (1)

ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

Solicitation Status

Endorsement Policy

ENDORSEMENT STATUS

PT Pelabuhan Indonesia (Persero)	EU Endorsed, UK Endorsed

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