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Sri Trang Agro-Industry Public Company Limited

Company Rating:

BBB+

Rating Outlook:

Stable

Rating Rationale

TRIS Rating assigns the company rating of Sri Trang Agro-Industry PLC (STA) at “BBB+”. The rating reflects the company’s strong market position in the natural rubber business, geographic diversity in terms of sales, hedging and back-to-back buying and selling strategy to partially mitigate price risk, in-depth knowledge of the natural rubber (NR) industry, and capable management. However, these strengths are partially offset by the natural rubber price fluctuations, highly competitive market conditions, and STA’s high financial leverage, although partially mitigated by liquid marketable inventories.

STA is a processor and trader of natural rubber. The company has 15 processing plants located in the south of Thailand and one in Indonesia with total capacity of 746,543 tonnes per year. The company’s market share in the global NR industry in the first three months of 2009 was 8.14% with trading volume of 166,317 tonnes, up from 7.46% in the same period of the prior year. Due to years of experience in the NR industry, STA’s management has been able to manage the company through the business cycles and has been able to sustain STA’s market position. Approximately 82% of its products were sold to the tire manufacturing industry; four of STA’s top five customers are tire manufacturers. Although sales are concentrated in a single industry, it is fairly diversified in terms of geography. The company also expanded customer base to small- and medium-sized tire manufacturers. Exports accounted for 79% of total sales in 2008. Approximately 62% of export sales were to customers in Asia; mainly China, Singapore, Japan and Korea; and about 10% and 9% were to customers in Europe and the United States.

Currently, the world’s major NR producers are Thailand, Indonesia and Malaysia. In 2008, the three countries accounted for 70% of global production of 9.9 million tonnes. Thailand was the largest producer, with total production volume of 3.09 million tonnes, followed by Indonesia (2.75 million tonnes) and Malaysia (1.08 million tonnes). NR is used as a raw material in various industries, including tires, surgical gloves, condoms, and footwear. Global NR consumption has grown steadily during the past decade. However, in 2008, global NR consumption declined to 9.7 million tonnes, compared with 9.9 million tonnes in 2007. Demand for NR declined sharply in the fourth quarter of 2008 due to the automotive industry slump which suffered from the credit crunch and the economic downturn. A sharp decline in vehicle demand also affected tire demand. Tire manufacturers were by far the largest end-users of NR, as they consume approximately 70% of global production.

The NR processing industry is labor intensive. Raw material costs account for approximately 90%-95% of the processing costs. Processors are highly exposed to volatile NR prices, and as a result, earnings and cash flow tend to fluctuate. To mitigate price risk and stabilize earnings and cash flow, STA adjusted its marketing strategy to the back-to-back selling and buying strategy and to have more direct contact with end-users and farmers. However, price risk is unavoidable during periods of high rubber price volatility.

STA reported a solid operating performance in 2008 despite an abrupt decline in sale volume and a collapse of NR prices in the fourth quarter of 2008. Net profit was Bt1,315 million before provision for diminution in value of inventories of Bt688 million. The profit was the highest for the past five years. Operating margin before depreciation expense was 3.29%, up from 1.4% in 2007. However, adjusted operating margin before depreciation (excluding reversal on diminution in value of inventories) in the first half of 2009 was 0.15%, down from 3.15% in the same period of the prior year. The lower margin reflected the high-cost inventories carried forward from 2008. Nonetheless, it is expected that the operating margin for

the rest of the year will be back to normal as all high-cost inventory was sold in the first quarter of 2009. As of June 2009, total debt was Bt8,327 million, down from Bt13,085 million as of June 2008. The total debt to capitalization ratio was 58.50%, down from 73.52% as of June 2008. The earnings before interest, tax, depreciation and amortization (EBITDA) interest coverage ratio in the first half of 2009 improved to 5.59 times, compared with 4.09 times in the same period of the prior year due to declining debt levels as well as falling interest rates.

Rating Outlook

The “stable” outlook reflects the expectation that STA will be able to maintain its strong market position in the NR business and has sufficient back up credit facilities from financial institutions. The company is expected to refrain from rubber price speculation, implement a conservative financial strategy and maintain the effective working capital management during a difficult industry environment.

Key Credit Considerations

Strengths/Opportunities

- Strong market position in natural rubber
- Geographic diversity in terms of sales
- Experienced management team with extensive industry knowledge
- Back-to-back buying and selling strategy to partially mitigate price risk
- High liquidity supported by liquid marketable inventory
- Countercyclical working capital profile

Weaknesses/Threats

- Highly competitive market conditions
- High financial leverage
- NR industry subject to high degrees of price volatility

Corporate Overview

STA was established in 1987 and listed on the Stock Exchange of Thailand (SET) in 1991. STA is one of the largest processors and exporters of natural rubber in Thailand. Paid up capital at the end of March 2009 was Bt1,000 million and net worth was Bt5,803 million. STA’s major shareholder is the Sincharoenkul family, with direct and indirect holding of a 35.57% stake as of December 2008.

STA has invested in 20 subsidiaries and affiliates that engage in both downstream and upstream businesses related to NR. The company started to diversify into downstream business in 1989 through joint ventures (JV) with the Austrian company, Semperit Technische Produkte Gesellschaft m.b.h (STPG), to produce rubber gloves, and currently has investments in five downstream companies. For upstream businesses, the company operates rubber and oil

palm plantation on approximately 300 rai in Trang and Songkhla provinces.

The STA group has 15 processing facilities located in the southern part of the country and one facility in Indonesia. Currently, total production capacity is 746,543 tonnes per year, comprising 198,000 tonnes of rubber smoked sheet (RSS), 316,600 tonnes of block rubber (STR) and 234,943 tonnes of concentrated latex. In 2008, STA had total sales of Bt60,134 million. The company exported 532,110 tonnes out of the 675,681 tonnes it sold in 2008, accounting for 79% of total sales volume.

INDUSTRY ANALYSIS

Natural rubber, also known as Para rubber, is an important agricultural export from Thailand. In 2008, rubber exports were the highest foreign exchange earner for the country, followed by rice. Thailand is the world’s largest natural rubber exporter. Rubber is the main agricultural product of the southern region, and production is being extended into other regions of Thailand. The rubber supply is seasonal, as lower production occurs when rubber trees shed leaves every summer. As with other agricultural products, rubber production is uncertain and varies with weather conditions. An investment in rubber trees is long-term by nature. The trees will begin to yield in the seventh year after planting, remain productive for approximately 15-23 years, and then will be cut and sold as rubber wood.

- *Natural rubber used mainly by vehicle tire producers*

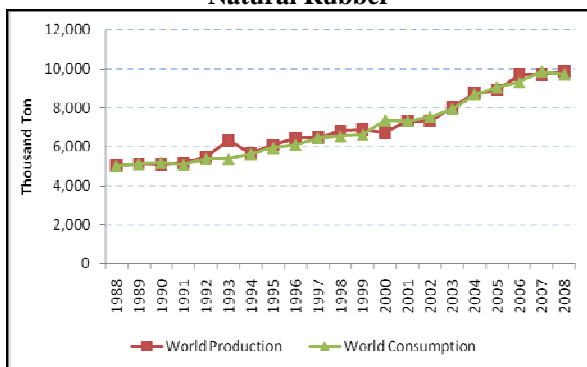
Due to the high elasticity, long fatigue life and good resistance to abrasion, natural rubber is used widely, in products ranging from household goods to industrial products. Rubber enters the

production stream at the intermediate stage or as the final product. The major finished products that require rubber as a feedstock are tires and latex gloves. Since automobile tire manufacturers use 60%-70% of all produced natural rubber, rubber demand is related to demand for vehicle tires. Tires can be classified into replacement tires and new tires, where demand is based on need from vehicle usage and vehicle manufacturers. Replacement tires account for approximately 70% of total tires sold and 75% of sales value. Demand in the replacement market is generally more stable than demand in the original equipment manufacturer (OEM) segment, because the latter is related to the cyclicity of the new vehicles market.

▪ **Sluggish economy cuts vehicle production and tire demand**

According to the Organisation Internationale des Constructeurs d'Automobiles (OICA), which is the association of global automobile manufacturers, world motor vehicle production decreased by 3.7% in 2008. Vehicle production reached 70.5 million units in 2008. The world economic crisis has dampened the automotive market worldwide. The world economy was projected to decline by 1.4% in 2009, according to the International Monetary Fund (IMF). In addition, the global economic downturn also has slowed demand for replacement tires.

Chart 1: World Production and Consumption of Natural Rubber



Source: The International Rubber Study Group (IRSG)

According to the International Rubber Study Group (IRSG), world natural rubber consumption in 2008 reached 9.7 million tonnes, a drop of 1.6% from 2007. The fall in consumption, the first drop in seven years, was in sharp contrast to the average annual growth of 5.1% during 2002-2007. In the first quarter of 2009, rubber consumption dropped by

approximately 17.5% year-on-year (y-o-y) as the global economic outlook remained weak. In 2008, China accounted for 26.3% of world consumption, followed by the United States (10.7%), India (9.1%) and Japan (9.0%). China has been the world's largest rubber consumer, overtaking the United States in 2001. In Thailand, domestic consumption of natural rubber was 397.6 thousand tonnes in 2008, up 6.4% from 2007. As rubber mostly serves as a raw material for the tire industry, the main consumers are leading tire manufacturers, e.g., Michelin, Bridgestone, Goodyear, and Continental, with manufacturing plants worldwide.

Natural rubber has been substituted, but not completely, by synthetic rubber, which is manufactured from oil. As oil prices rise, so does the price of synthetic rubber. According to the IRSG, at the end of 2008, synthetic rubber consumption throughout the world declined to 12.6 million tonnes from 13.2 million tonnes in 2007. The share of natural rubber consumption increased to 43.6% of total rubber consumed in 2008, up from 41.6% in 2002, in line with rising trend of oil prices. However, the consumption trend will reverse when the natural rubber price is comparatively high. High prices and worries about long-term availability of natural rubber may induce further substitution.

▪ **Thailand is world's largest rubber producer**

In 2008, Thailand cultivated rubber trees on 16.72 million rai nationwide. Of that amount, 68%, or 11.37 million rai are harvested areas. Due to rising rubber prices and government support for the expansion of rubber plantations during the past four years, the cultivated area grew rapidly by 5.0%-8.8% per year in 2005-2008, greater than the 0.7%-2.7% annual growth rates for 2003-2004. However, the harvested area grew more slowly at 1.5%-3.5% per year. Rubber production in 2008 was 3.09 million tonnes, up 0.98% from 2007. The annual rubber yield in 2008 was 278 kilograms (kg.) per rai, up 1.8% from 2007. Despite the recent rise in production in 2008, the drop in demand resulting from global economic downturn will probably affect production. Thus, rubber production in Thailand during 2009 will probably decline from earlier estimates.

There are three main types of natural rubber products in Thailand: ribbed smoked sheet (RSS), block rubber or Standard Thai Rubber (STR) and concentrated latex. Both

RSS and STR are used primarily in tire manufacturing while concentrated latex is used in the latex glove industry. Due to the increasing demand for STR from tire producers in recent years, production in Thailand has shifted to focus more on STR since 2005. According to the Rubber Research Institute of Thailand (RRIT), STR accounted for 41% of total production in 2008, and the production share of RSS and concentrated latex were 31% and 19%, respectively. In Thailand, there are many natural rubber exporters. However, the market is high concentrated. According to the Thai Rubber Association (TRA), the five largest rubber exporters shipped 51% of rubber export in 2008. Von Bundit, the market leader, controlled 15.3%, followed by Sri Trang Agro-Industry, Southland Group, Thai Hua Rubber and Thaitech Rubber Corporation, with shares of 10.9%, 10.8%, 7.5% and 6.0%, respectively.

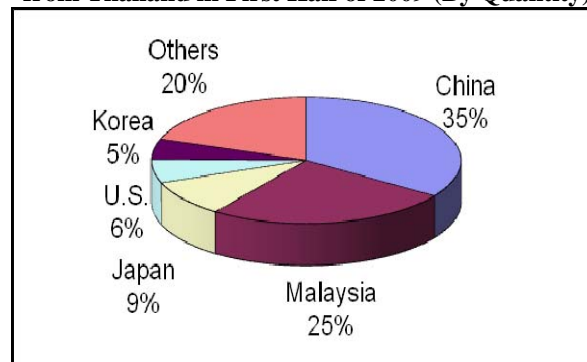
Asia has remained the dominant source of natural rubber in the world. According to the IRSG, Asia accounted for 95.2% of the global supply of natural rubber in 2008. The majority of the natural rubber was originated in Thailand, Indonesia and Malaysia. In 2008, Thailand was the largest supplier, providing 31.3% of the world supply, followed by Indonesia and Malaysia with 27.9% and 10.9%, respectively.

▪ ***Thailand and Indonesia rubber exports dropped in 2008 and the first quarter of 2009***

During 2002-2008, among the agricultural products in Thailand, rubber was the most important export product. In 2008, the export value of rubber was US\$6,791.7 million, approximately US\$587.6 million greater than that of rice, the second most successful agricultural product. Thailand has been the world's largest natural rubber exporter since 1991. Approximately 90% of Thailand's rubber production has been exported, mainly to China, Malaysia, Japan, the United States and South Korea. The recovery of the Chinese economy in 2009 is expected to make the amount of rubber exported to China increase in 2009 and 2010. In 2008, Thailand exported 2.7 million tonnes of rubber, a drop of 1.1% from 2007. Rubber exports from Indonesia, the second largest producer and exporter, contracted by 4.6% to 2.3 million tonnes in 2008. In the first quarter of 2009, rubber exports from Thailand and Indonesia dipped by -14.3% y-o-y and -17.0% y-o-y, respectively.

The strengthening of the baht has decreased the revenue of Thai producers and exporters. The continuing and rapid appreciation of the baht may lower the nation's competitiveness and damage export markets for Thai products.

Chart 2: Export Markets for Natural Rubber from Thailand in First Half of 2009 (By Quantity)



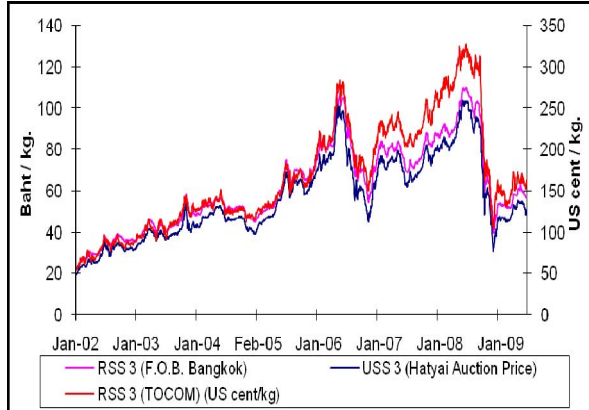
Source: Ministry of Commerce

▪ ***High price volatility in rubber trading***

As natural rubber is a global commodity, rubber prices reflect the worldwide demand-supply balance. The prices of natural rubber are volatile for three reasons: price speculation, the substitution of synthetic or man-made rubber due to oil price change, and the inability to increase the amount of harvested rubber in the short run. Thai rubber prices in the physical market comprise various auction prices, such as unsmoked sheet grade 3 (USS3) Hatyai and RSS grade 3 (RSS3) Hatyai, and official noon prices, such as RSS3 F.O.B. Bangkok. In addition to the physical market, rubber is also traded in commodity future markets, e.g., the Tokyo Commodity Exchange (TOCOM), the Singapore Commodity Exchange (SICOM), Shanghai Futures Exchange (SHFE), and the Agricultural Futures Exchange of Thailand (AFET). With good access to price information for all market participants, prices in all markets have shown the same patterns. Natural rubber prices rose between 2002 and mid-2008, due to higher demand plus rising oil prices and an expanding world economy. The price volatility has been higher since 2006. The average price of RSS grade 3 (F.O.B. Bangkok) increased to Bt87.21 per kg. in 2008 from Bt78.44 per kg. in 2007. After much price fluctuation in 2006, the price continued to increase and peaked at Bt110.20 per kg. in July 2008, before slipping to Bt39.40 per kg. in December 2008. This significant price volatility was mainly influenced by falling demand resulting from the global

economic downturn. In the first six months of 2009, the price remained low and averaged at Bt55.81 per kg. due to the slower economic growth of China and the uncertain outlook of the world economy.

Chart 3: Natural Rubber Price Movement



Source: The Rubber Research Institute of Thailand (RRIT)

▪ **Government regulations and policies**

The rubber industry in Thailand is regulated by two main laws: the Rubber Act B.E. 2549 and the Rubber Replanting Aid Fund Act B.E. 2503. The Rubber Act B.E. 2549 controls all rubber market activities, including strain, planting, cultivation zones, shipment, processing, and trading. The Office of Rubber Replanting Aid Fund was established on 5 December 1960 by The Rubber Replanting Aid Fund Act B.E. 2503. The objective of this law is to help owners of rubber plantations with low productivity in two ways: by granting aid funds for replanting and by breeding good rubber trees in order to replace old trees. The source of the funds is deposits from the collection of *cess* on exports of natural rubber. Currently, rubber exporters are required by law to pay the *cess* rate at Bt1.40 per kg.

The Ministry of Agriculture and Cooperatives (MOAC) has encouraged the rubber industry in Thailand. In planting, authorities emphasize both area expansion and productivity improvement. The Thai government had a project to increase the new planting area by 1 million rai during 2004-2007. Thirty percent of the new growing areas was to be in the North and 70% in the Northeast. In addition, MOAC has approved a road map and strategy for increasing natural rubber production and encouraging the use of rubber-based products. This project also has emphasized technology development to increase planting productivity and the value of rubber products.

BUSINESS ANALYSIS

STA is engaged in processing, distributing and marketing NR products. The company's competitive position stems from its strong market position in NR processing and an extensive network of raw material sources, good relationships with customers, and an experienced management team that has in-depth industry knowledge.

▪ **Strong market position**

STA is one of the largest natural rubber processors and exporters in Thailand. In 2008, Thailand produced 3.09 million tonnes of rubber and export volume was 2.68 million tonnes. STA's total production capacity in 2008 was 683,634 tonnes. Its actual production volume in 2008 was 456,403 tonnes, comprising 105,752 tonnes of RSS, 254,829 tonnes of STR and 95,822 tonnes of concentrated latex, accounting for 15% of Thailand's total production. The company plans to expand block rubber production in the northeastern part of the country.

Table 1: STA's Production and Domestic Market Shares

Unit: Tonnes

Production	2004	2005	2006	2007	2008
RSS	124,639	104,779	102,289	115,529	105,752
STR	125,101	136,647	140,381	212,809	254,829
Concentrated latex	124,226	113,339	130,687	129,626	95,822
Total	373,966	354,765	373,357	457,964	456,403

Unit: %

Domestic Market Share	2004	2005	2006	2007	2008
RSS	11.29	10.42	9.94	12.07	10.87
STR	11.03	11.02	11.78	17.47	19.88
Concentrated latex	21.02	19.36	18.72	19.52	16.32

Sources: STA and TRIS Rating

Table 2: Production of Rubber Products in Thailand

Unit: Tonnes

Production	2004	2005	2006	2007	2008
RSS	1,104,180	1,005,700	1,028,930	957,337	973,243
STR	1,134,030	1,240,265	1,192,055	1,218,326	1,282,036
Concentrated latex	590,890	585,300	697,980	663,926	587,047
Compound	86,544	36,715	138,163	151,437	154,485
Others	68,649	69,178	79,865	64,979	92,910
Total	2,984,293	2,937,158	3,136,993	3,056,005	3,089,721

Source: Rubber Research Institute of Thailand

Supplies of natural rubber are fragmented, as rubber plantations in Thailand are mainly operated by small-hold farmers. The market is

highly competitive and farmers are kept well informed of price movements by Thai government agencies. Traditionally, NR processors purchase raw materials from intermediaries. STA has made an effort to purchase raw materials directly from farmers by setting up purchasing centers to gain knowledge about actual supply in the market and to strengthen its supply network. Presently STA operates 25 purchasing centers in districts and sub-districts in Thailand's southern and northeastern provinces.

STA purchases approximately 65% of its unprocessed rubber and rubber sheet directly from farmers (including cooperatives and company purchasing centers), with the remaining 35% indirectly purchased through intermediaries. The company is not dependent on any particular supplier. Currently, STA has more than 400 suppliers, spread throughout the southern region of the country. Purchases are made on a daily basis and by cash only. In 2008, STA purchased a total of 549,734 tonnes of unprocessed rubber and rubber sheet.

▪ ***Sales are concentrated in the tire industry, but are diversified by geography***

In 2008, STA had around 7% global market share for NR products, selling 675,681 tonnes, of which 62% was block rubber (STR and Standard Indonesian Rubber (SIR)), 23% was RSS, 15% was concentrated latex and 1% was other rubber products. RSS, STR and SIR are sold mainly to tire manufacturers, including Michelin, Bridgestone, Goodyear, Continental, Hankook, and Yokohama. Concentrated latex is sold mainly to an affiliated company, Siam Sempermed Corporation Ltd. (SSC), which took approximately 33% of total concentrated latex sales. The top five customers accounted for 31% of total sales value in 2008. The largest customer in 2008 was Goodyear, which accounted for 8% of total sales value.

STA exported approximately 85% of total sales in the first quarter of 2009, up from 79% in 2008. Its largest export market was Taiwan/China, which represented 47% of total exports in the first quarter of 2009, up from 37% in 2008. The strong sales growth in China is the result of stationing marketing team in Shanghai and Qingdao and because of the high growth of the Chinese market. In addition, the company set up a storage and distribution center in Qingdao to facilitate prompt delivery to customers. This will also allow STA to expand the customer base to small- and medium-sized

customers. Singapore was the second largest export market in the first quarter of 2009, accounting for 16% of total exports, down from 17% in 2008. The third and the fourth largest export markets were the United States and Japan, accounting for 9% and 8%, respectively, of total exports.

Table 3: STA's Export Sales by Geographic Area

Unit: tonnes

	2007	2008	Jan-Mar 2009
China	197,699	195,389	66,328
Singapore	111,202	91,635	22,180
Europe	58,631	53,397	7,732
USA	49,188	48,788	13,233
Malaysia	43,858	5,283	2,421
Japan	37,565	50,652	10,863
Korea	32,918	41,698	7,681
India	25,694	16,517	2,457
Others	15,577	28,751	8,946
Total export	572,332	532,110	141,841

Source: STA

▪ ***Hedging and daily sales and purchase strategy should partially mitigate price risk***

Since the price of NR is quite volatile, STA uses as much as possible, the back-to-back selling and buying strategy in order to mitigate the risk of price fluctuations. This should stabilize operating performance. STA changed its marketing strategy from selling through agents to selling directly to end-users. The strategy helps the company gain a better understanding of actual demand and business sentiment, which allows the company to efficiently manage production and inventory levels. After several contracts unwound in the fourth quarter of 2008, the company changed its selling strategy in 2009 from traditional long-term price adjustable contracts to spot contracts for most of its customers. The company will fix the price for forward delivery against its own costs. This differs from its past practice which used the average of the daily SICOM price in a single month. Orders will be settled with inventory on hand. STA typically maintains inventory equal to approximately one to two months of sales.

The sales and purchase mechanisms should minimize price risk and stabilize the company's margin. However, the company is still exposed to margin volatility should there be a large swing in NR prices. STA's management confirms that the company has no policy of engaging in speculative trading. The company does not enter into sales orders without physically securing the NR. Futures market operations are merely to mitigate price risk.

▪ **Diversified production facility to Indonesia**

STA invested in a production facility in Indonesia to weather unpredictable factors that might affect raw material supplies in Thailand. However, the production capacity in Indonesia is relatively small, at only approximately 6% of total group production capacity. Currently, the company is in the process of acquiring a block rubber production plant to expand production capacity. The diversification of production to Indonesia allows STA to take advantage of price differentials among markets and provides it with in-depth information about NR supply in Indonesia, which is the largest NR plantation country. Currently, Indonesia is the second largest producer and exporter of NR in the world.

▪ **Expanded by setting up trading companies in foreign countries**

In 2002, STA established a trading company, Sri Trang International Pte Ltd. (STI), in Singapore, as Singapore is the world's biggest NR trading hub and price-discovery center. Every major tire manufacturers has purchasing offices in Singapore to source and buy NR. STA, through its subsidiary, STI, secures products, particularly SIR, from other producers to supply to its customers.

Since the establishment of STI, the group's sales volume has increased significantly from 297,473 tonnes in 2002 to 675,681 tonnes in 2008.

Apart from STI, STA also established Sri Trang USA, Inc (STU) to cover trading in the United States. However, the trading volume through STU is still low. The company is planning to establish a new sales office in China to strengthen its position in China. For the first three months of 2009, STA's market share in China was 11.11%, up from 7.63% in 2008.

▪ **FX risks is partially mitigated through pricing mechanism and forward contract**

Approximately 80% of STA's total revenues are in US\$ while payments to the farmers for raw materials are in Thai baht. However, the pricing of raw materials are based on international prices quoted in US\$ and Japanese yen. Currently, domestic NR prices are determined by reference to prices in both the international and local markets, such as TOCOM, SICOM, AFET and the domestic auction market run by the Rubber Research

Institute of Thailand (RRIT). The company does not fully hedge against foreign exchange fluctuation. Foreign exchange risks are also partially mitigated through the international price quotations. Forward contracts are also used to protect against currency exchange risks.

▪ **Capable management team**

STA's management team, headed by Dr. Viyavood Sincharoenkul, has a wealth of experience and extensive industry knowledge. This is proven by the successful track record of managing the company through many price fluctuation cycles. STA's founders are key members of management, with more than 30 years of experience in the NR industry.

In addition, Dr. Viyavood, the company's managing director, is a board members of SICOM and the only Thai on the board.

▪ **Diversified to downstream businesses**

STA diversified into downstream businesses through JV with an Austrian company, STPG. The first JV company, SSC, was established in 1989 to manufacture latex examination gloves. STA's stake in SSC is 36%. Currently, SSC is one of STA's top five customers. In 1996, the two partners established Semperflex Asia Co., Ltd. and Semperform Pacific Co., Ltd., with STA taking a 40% stake in each company. The companies manufacture high pressure hydraulic hoses and rubber and plastic parts, respectively. Semperflex Shanghai was established in 2005 to manufacture hydraulic hoses in China. STPG provides technical know-how and research and development (R&D) to the JV companies, while STA runs the operations in Thailand. STA received Bt102 million in dividend income from associated companies involving downstream businesses in 2008.

Table 4: STA's Dividend Income from Associated Companies in Downstream Businesses

Unit: Bt million

	2003	2004	2005	2006	2007	2008
Siam Sempermed Co., Ltd.	160.92	120.69	80.46	-	-	80.46
Semperflex Asia Co., Ltd.	59.50	42.50	25.50	-	-	21.25
Total	220.42	163.19	105.96	-	-	101.71

Source: STA

FINANCIAL ANALYSIS

STA's financial profile is driven by the nature of agricultural commodity products

with thin margins, high leverage and volatile cash flow.

▪ ***Strong operating performance despite natural rubber price volatility***

STA reported solid operating performance in 2008 despite an abrupt decline in sales volumes and the collapse of NR prices in the fourth quarter of 2008. Net profit was Bt1,315 million before provision for diminution in value of inventories of Bt688 million. This was the highest profit over the past five years. Operating margin before depreciation expense was 3.29%, up from 1.4% in 2007. The high variable production costs structure allows the company to curtail production to better align output with the sharp decline in orders in the fourth quarter of the year. The strategy to sell directly to end-users helps the company gauge demand more accurately, avoiding high inventory costs as NR prices fell. Inventory days as at December 2008 were down to 33 days compared with inventory turnover of 56 days and 62 days in 2007 and 2006, respectively.

After the very weak sales volume in the fourth quarter of 2008, orders resumed moderately in the first half of 2009 to 350,474 tonnes, down by 1.7% y-o-y. Adjusted operating margin before depreciation (excluding reversal on diminution in value of inventory) was 0.15%, down from 3.15% in the same period of the prior year. The decline margin reflected the high-priced inventories. Nonetheless, it is expected that the operating margin for the rest of the year will be back to normal as all high-cost inventory was sold in the first quarter.

▪ ***Working capital requirement counters industry cycle***

STA's working capital requirement is countercyclical. The lower sales volumes and selling prices for NR rubber will result in a reduction of the working capital requirements, reducing outstanding debts. Usually the company's working capital requirement will peak during the first and the fourth quarter of the year, in line with the seasonality of tapping in Thailand. STA finances its working capital with short-term loans from financial institutions. As of June 2009, STA's total debt was Bt8,327 million, compared with Bt13,085 million in the same period of the previous year.

The lower debt level was mainly due to a steep decline in NR prices and lower sale volumes. Most of STA's borrowings were used to fund trade finance transactions that are self liquidating. As of June 2009, 58% of all outstanding loans were used to finance inventory; 29% were used to finance trade receivables. As of June 2009, the total debt to capitalization ratio was 58.5%, down from 61.76% as of December 2008 and 73.52% as of June 2008.

▪ ***Cash flow protection weak but partly mitigated by liquid marketable inventory***

While STA's cash flow protection is weak due to its high financial leverage, it is partly mitigated by low capital expenditures and liquid marketable inventory that can be easily liquidated in a stress situation. The adjusted funds from operations (FFO) to total debt ratio improved substantially from 1.91% in 2007 to 19.94% in 2008, due to a significant decline in total debt in the fourth quarter of 2008 in line with lower business activity. However, the adjusted FFO in the first half of 2009 was negative as a result of the effect of high inventory costs carried forward from 2008. Thus, the FFO to total debt ratio was -2.7% (non-annualized). The EBITDA interest coverage ratio in the first half of 2009 improved to 5.59 times, compared with 4.09 times in the same period of the prior year due to declining debt levels as well as lower interest rates.

▪ ***Strong financial flexibility***

STA's financial flexibility is strong, backed by cash on hand, commercial bank back-up credit facilities, and liquid marketable inventory. At the end of June 2009, the group had approximately Bt20 billion in uncommitted working capital credit facilities from 21 banks; only 40% has been utilized. The company had Bt1,187 million of unrestricted cash and marketable securities. The company also had Bt4,800 million in inventory (marked to market) of which Bt3,300 million were finished goods, Bt1,441 million was work in progress and raw materials, and Bt59 million was others.

Financial Statistics and Key Financial Ratios*
Unit: Bt million

	Jan-Jun 2009	----- Year ended 31 December -----				
		2008	2007	2006	2005	2004
Sales	19,060	60,134	50,017	39,034	28,847	27,454
Gross interest expense	168	651	561	542	252	189
Net income from operations	564	627	108	582	(173)	712
Funds from operations (FFO)	(495)	1,688	233	865	(48)	760
Adjusted funds from operations (Adj. FFO)**	(224)	1,790	233	865	78	939
Capital expenditures	249	632	462	470	432	402
Inventories	4,800	4,433	7,361	6,189	5,096	4,151
Total assets	15,519	15,265	18,015	14,756	12,546	11,158
Total debt	8,327	8,976	12,219	9,468	7,552	6,302
Shareholders' equity	5,908	5,559	4,005	4,161	4,285	4,036
Operating income before depreciation and amortization as a % of sales	3.74	3.29	1.40	3.63	0.41	3.00
Pretax return on permanent capital (%)	5.37***	8.53	4.72	10.01	1.72	10.40
Earnings before interest, tax, depreciation and amortization (EBITDA) interest coverage (times)	5.59	2.47	1.74	2.79	1.63	6.33
FFO/total debt (%)	(5.94)***	18.81	1.91	9.14	(0.63)	12.06
Adj. FFO/total debt (%)	(2.70)***	19.94	1.91	9.14	1.03	14.89
Total debt/capitalization+short-term debt (%)	58.50	61.76	75.31	69.47	63.80	60.96

* Consolidated financial statements

** Adjusted by including dividend income from associated companies

*** Non-annualized

Rating Symbols and Definitions

TRIS Rating uses eight letter rating symbols for announcing medium- and long-term credit ratings. The ratings range from AAA, the highest rating, to D, the lowest rating. The medium- and long-term debt instrument covers the period of time from one year up. The definitions are:

- AAA** The highest rating, indicating a company or a debt instrument with smallest degree of credit risk. The company has extremely strong capacity to pay interest and repay principal on time, and is unlikely to be affected by adverse changes in business, economic or other external conditions.
- AA** The rating indicates a company or a debt instrument with a very low degree of credit risk. The company has very strong capacity to pay interest and repay principal on time, but is somewhat more susceptible to the adverse changes in business, economic, or other external conditions than AAA rating.
- A** The rating indicates a company or a debt instrument with a low credit risk. The company has strong capacity to pay interest and repay principal on time, but is more susceptible to adverse changes in business, economic or other external conditions than debt in higher-rated categories.
- BBB** The rating indicates a company or a debt instrument with moderate credit risk. The company has adequate capacity to pay interest and repay principal on time, but is more vulnerable to adverse changes in business, economic or other external conditions and is more likely to have a weakened capacity to pay interest and repay principal than debt in higher-rated categories.
- BB** The rating indicates a company or a debt instrument with a high credit risk. The company has less than moderate capacity to pay interest and repay principal on time, and can be significantly affected by adverse changes in business, economic or other external conditions, leading to inadequate capacity to pay interest and repay principal.
- B** The rating indicates a company or a debt instrument with a very high credit risk. The company has low capacity to pay interest and repay principal on time. Adverse changes in business, economic or other external conditions could lead to inability or unwillingness to pay interest and repay principal.
- C** The rating indicates a company or a debt instrument with the highest risk of default. The company has a significant inability to pay interest and repay principal on time, and is dependent upon favourable business, economic or other external conditions to meet its obligations.
- D** The rating for a company or a debt instrument for which payment is in default.

The ratings from AA to C may be modified by the addition of a plus (+) or minus (-) sign to show relative standing within a rating category.

TRIS Rating's short-term ratings focus entirely on the likelihood of default and do not focus on recovery in the event of default. Each of TRIS Rating's short-term debt instrument covers the period of not more than one year. The symbols and definitions for short-term ratings are as follows:

- T1** Issuer has strong market position, wide margin of financial protection, appropriate liquidity and other measures of superior investor protection. Issuer designated with a "+" has a higher degree of these protections.
- T2** Issuer has secure market position, sound financial fundamentals and satisfactory ability to repay short-term obligations.
- T3** Issuer has acceptable capacity for meeting its short-term obligations.
- T4** Issuer has weak capacity for meeting its short-term obligations.
- D** The rating for an issuer for which payment is in default.

All ratings assigned by TRIS Rating are local currency ratings; they reflect the Thai issuers' ability to service their debt obligations, excluding the risk of convertibility of the Thai baht payments into foreign currencies.

TRIS Rating also assigns a "**Rating Outlook**" that reflects the potential direction of a credit rating over the medium to long term. In formulating the outlook, TRIS Rating will consider the prospects for the rated company's industry, as well as business conditions that might have an impact on the fundamental creditworthiness of the company. The rating outlook will be announced in conjunction with the credit rating. In most cases, the outlook of each debt obligation is equal to the outlook assigned to the issuer or the obligor. The categories for "**Rating Outlook**" are as follows:

- Positive** The rating may be raised.
- Stable** The rating is not likely to change.
- Negative** The rating may be lowered.
- Developing** The rating may be raised, lowered or remain unchanged.

TRIS Rating may announce a "**CreditAlert**" as a part of its monitoring process of a publicly announced credit rating when there is a significant event that TRIS Rating considers to potentially exerting a substantial impact on business or financial profiles of the rated entity. Due to an insufficient data or incomplete developments of the event, such as merger, new investment, capital restructuring, and etc., current credit rating remains unchanged. The announcement aims to forewarn investors to take a more cautious stance in investment decision against debt instruments of the rated entity. CreditAlert report consists of a "Rational" indicating warning reasons, a "CreditAlert Designation", and a current credit rating. Rating Outlook is withheld in the announcement.

CreditAlert Designation illustrates a short-term rating outlook indicative of the characteristics of impacts on the credit rating in one of the three directions (1) *Positive* (2) *Negative* and (3) *Developing*.

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