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Research Update:

PT Bayan Resources Tbk. Assigned 'B+' Rating; Outlook Stable

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Overview

- Bayan faces single mineral and mine concentration, and has a small scale relative to global peers. The company's low cost position, long reserve life, and adequate liquidity partly offset these risks.
- We believe Bayan's leverage will remain modest, even in a less favorable pricing scenario, because the company has fully repaid its outstanding term loans and established two new lines of credit.
- We are assigning our 'B+' long-term issuer credit rating to Bayan, an Indonesia-based coal mining company.
- The stable outlook reflects our expectation that Bayan has satisfactory debt servicing ability over the next 12 months.

Rating Action

On Sept. 12, 2018, S&P Global Ratings assigned its 'B+' long-term issuer credit rating to PT Bayan Resources Tbk. (Bayan). The outlook is stable. Bayan is an Indonesia-based holding company that has majority ownership in operating companies with coal mining concessions in Indonesia.

Rationale

The rating reflects Bayan's single mine and mineral exposure, and limited scale relative to global coal producers. The company faces the risk of fluctuations in working capital during the dry season, and its credit ratios are sensitive to volatility in coal prices. Mitigating these risks are the sound cost position and long reserve life of Bayan's mines, the company's adequate liquidity, and the likelihood it will continue to generate positive discretionary cash flows through 2020.

We expect the Tabang/Pakar mines to account for about 70% of Bayan's production. This site is inland in East Kalimantan, and is dependent on fully owned infrastructure for distribution. Specifically, barging down the Kedang Kepala River can be delayed during the dry season, and has delayed sales in the past. Bayan is building a new haul road to the Mahakam River to mitigate this risk; however, the road is not likely to be complete until 2021. The company produced about 20 million metric tons (MMT) of coal in 2017, up from 10 MMT in 2016, and expects to increase annual production to 25 MMT-28 MMT in 2018 and beyond. This rapid growth is primarily due to increasing production at Bara Tabang.

Bayan's operations should continue to have low mining costs, driven by moderate stripping ratios of 3.5x-4.5x on average. This translates into group overburden removal costs of about US$10 per ton, with all-in cash costs averaging US$28-US$31 per ton across all operations. We project the cost and average strip ratios to be stable over the next 12-24 months. The Bara Tabang mine is in the first quartile of the global energy adjusted cash cost curve, and compares favorably with other large or midsize coal mines in Indonesia.

Bayan sells a low-energy-content product and its average selling price is typically about 40% below the Newcastle thermal coal FOB benchmark. We project Bayan's average selling prices to be US$45-US$55 per ton over the next few years, which is lower than that of Indonesia peers PT Berau Coal Indonesia, PT Bumi Resources, PT Kideco Jaya Agung, and PT Indo Tambangraya Megah Tbk. However, Bayan has a lower cost base per ton and we forecast its EBITDA per ton to be US$15-US$20 per ton on average, which is comparable or better than that of the Indonesian peers. Additionally, its profit and margins should be more resilient in a downturn than that of peers with a higher energy content product and higher cost base.

Although less important than profitability, Bayan has other characteristics which compare favorably to peers'. The reserve life at the Tabang/Pakar deposit is about 30 years with 800 MMT of reserves (including Kangaroo Resources Ltd.), which provides good potential for growth in production. Additionally, Bayan enters into sales contracts with end users to provide visibility over offtake. The company has contracted its entire expected production in 2018 and about 50% for the next five years, resulting in lower reliance on commodity traders than its peers do. Additionally, 69% of 2018 production is contracted at fixed prices, which helps reduce price volatility.

Bayan's increased production in 2017 resulted in positive cash flows for debt repayment. The company raised production at the low-cost Bara Tabang and Fajar Sakti sites to 15.6 MMT in 2017, from 6.1 MMT in 2016. This helped drive an increase in total production to 20.9 MMT in 2017, from 9.7 MMT in 2016. The stronger operations continued in the first half of 2018, with an annual run rate of 29.6 MMT. The volume increases occurred amid favorable pricing, leading to EBITDA of US$485 million in 2017. Bayan used the cash flow, along with proceeds from a new US$100 million credit facility with Permata Bank, to fully prepay US$484 million of loans. The company's credit facility with Permata Bank complements a US$75 million facility recently established with Sumitomo Mitsui Banking Corp., which together provide liquidity.

We expect Bayan to maintain modest leverage and interest coverage with continued access to liquidity. We project the company's annual EBITDA will average US$250 million-US$350 million through a coal price cycle, with the ratio of funds from operations (FFO) to debt averaging about 50%.

We expect Bayan to maintain limited debt balances while fully funding capital expenditure using internal cash flows. The company's capital expenditure is manageable at under US$100 per year because the company's existing capacity does not require substantial additional investment. This allows for positive discretionary cash flows through 2020, while also paying a dividend of around half of the previous year's net income. The positive cash flows should lead to growing cash balances. Bayan also has access to a total of US$175 million across the two three-year credit facilities.

In our credit analysis, we do not net Bayan's sizable cash balance and excess cash accumulation in 2018 against its debt, given the volatility of coal prices. Nevertheless, we recognize that the company is likely to generate positive discretionary cash flows through 2020, translating into cash accumulation amid growing production. We believe that rising cash balances could provide the company with sufficient headroom against future extended periods of lower prices or working capital fluctuations. The prospect of a sound liquidity position support our assessment of Bayan's credit quality.

Our base case assumes the following:

- GDP growth of about 5% in the Asia-Pacific region in 2018 and 2019, and slightly higher in Indonesia.
- Volatile coal prices averaging US$90-US$100 in 2018, benchmarked to the Newcastle 6300.
- Bayan's total production of 25 MMT-26 MMT in 2018, rising to 26 MMT-27 MMT annually in subsequent years. The Tabang/Pakar mines would produce about 18 MMT this year, and 19 MMT in 2019 and beyond.
- Average cash cost per ton excluding interest of US$28-US$32.
- FFO of US$200 million in 2018, and US$250 million in 2019 and beyond, assuming increased production and normalized coal prices.
- Capital expenditure of less than US$100 million annually.
- Dividends of about 50% of prior year's income.

Based on these assumptions, we arrive at the following credit measures:

- Ratio of FFO to debt of about 600% in 2018 and 45%-60% through the coal price cycle.
- Ratio of debt to EBITDA of less than 0.5x in 2018 and 1.0x-2.0x through the cycle.
- FFO cash interest coverage of more than 50x in 2018 and 9x-13x through the cycle.

Liquidity

We assess Bayan's liquidity as adequate. We expect the company's liquidity sources to cover liquidity needs by over 1.2x over the 12 months ending June 2019. We expect Bayan's revolving credit availability, positive cash flows, and growing cash balances to ensure it faces no liquidity pressure.

Principal liquidity sources include:

- Cash balance of US$135 million as of June 30, 2018.
- Cash FFO that we estimate at US$300 million-US$350 million over the 12 months ending June 30, 2019.
- Available credit facilities of about US$75 million.

Principal liquidity uses include:

- Working capital outflows of US$15 million-US$20 million over the 12 months to June 2019.
- Capital expenditure of US$70 million-US$80 million over the period.
- Dividends of US$150 million-US$200 million over the period.
- Acquisition of the remaining shares in Kangaroo Resources for US$167 million.

Outlook

The stable outlook reflects our expectation that Bayan will be able to adequately service its debt over the next 12 months. The current supportive coal prices should provide steady cash flows and liquidity for the company. The stable outlook also reflects our expectation that Bayan's Bara Tabang operations will remain stable and profitable.

Downside scenario

We would lower the rating if Bayan's debt balance increases and liquidity weakens materially. This could result from a sharp fall in realized coal prices and profit per ton coinciding with acquisitions and elevated capital spending, while production declines, possibly due to delays or operational challenges. A debt-to-EBITDA ratio above 3x would indicate such deterioration.

Upside scenario

We would raise the rating if Bayan is able to diversify its operations, but we believe that is unlikely over the next 12 months. A higher rating could also be supported by more mine sites and a larger scale, progress on the Mahakam haul road, or diversification into uncorrelated businesses, while maintaining the current financial profile and liquidity position.

Ratings Score Snapshot

Issuer Credit Rating: B+/Stable/--

Business risk: Vulnerable

- Country risk: High

- Industry risk: Moderately high
- Competitive position: Vulnerable

Financial risk: Modest
- Cash flow/Leverage: Minimal

Anchor: bb-

Modifiers
- Diversification/Portfolio effect: Neutral (No impact)
- Capital structure: Neutral (No impact)
- Liquidity: Adequate (No impact)
- Financial policy: Neutral (No impact)
- Management and governance: Fair (No impact)
- Comparable rating analysis: Negative (-1 notch)

Stand-alone credit profile: b+

Related Criteria

- General Criteria: Guarantee Criteria, Oct. 21, 2016
- Criteria - Corporates - General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- Criteria - Corporates - Industrials: Key Credit Factors For The Metals And Mining Upstream Industry, Dec. 20, 2013
- General Criteria: Group Rating Methodology, Nov. 19, 2013
- Criteria - Corporates - Industrials: Methodology For Standard & Poor's Metals And Mining Price Assumptions, Nov. 19, 2013
- Criteria - Corporates - General: Corporate Methodology: Ratios And Adjustments, Nov. 19, 2013
- Criteria - Corporates - General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers, Nov. 13, 2012
- General Criteria: Stand-Alone Credit Profiles: One Component Of A Rating, Oct. 1, 2010
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Ratings List

New Rating

PT Bayan Resources Tbk.	
Issuer Credit Rating	B+/Stable/--

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.

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