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HOME PRODUCT CENTER PLC

No. 166/2017 29 November 2017

Company Rating: A+

Outlook: Positive

Company Rating History:

Date	Rating	Outlook/Alert
18/11/11	A+	Stable
17/11/10	A	Positive
22/10/08	A	Stable
23/01/07	A-	Stable
15/10/04	BBB+	Stable
12/07/04	BBB	Positive
05/11/03	BBB	-

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Rating Rationale

TRIS Rating affirms the company rating of Home Product Center PLC (HMPRO) at "A+". At the same time, TRIS Rating revises upward the rating outlook of HMPRO to "positive" from "stable". The "positive" outlook reflects an expected improvement in HMPRO's profitability and cash flow generation, supported by a better product mix and efficient control of costs. The rating continues to reflect the company's leading position in the home improvement retailing industry in Thailand, satisfactory performance, and operating efficiencies. The rating also takes into consideration the intense nature of competition among modern home improvement retailers, the fragile recovery of the Thai economy, and ongoing low farm income.

HMPRO is Thailand's leading home improvement retailer. HMPRO operates two types of stores: HomePro stores and Mega Home stores. A HomePro store, the initial format, offers a wide range of home-related products and services in a store area of 2,500-12,000 square meters (sq.m.). A Mega Home store is a large-scale warehouse-style store in a store area of 12,000-20,000 sq.m. Mega Home stores are designed to be wholesalers and retailers of construction materials, home finishing products, and home improvement materials which will serve the needs of contractors, construction projects, resellers, and end-users. As of September 2017, HMPRO's major shareholders were Land & Houses PLC (LH; owning 30.2%) and Quality Houses PLC (QH; 19.9%).

The rating reflects the company's strong footprint in the modern home improvement retailing industry nationwide, a direct result of an ongoing expansion. At the end of September 2017, HMPRO owned and operated 101 stores, comprising 27 stores in Greater Bangkok, 57 stores upcountry, five stores in Malaysia, plus 12 Mega Home stores. During the first nine months of 2017, the company opened six new stores: two HomePro stores in Thailand, three HomePro stores in Malaysia, and one Mega Home store in Thailand. In addition, the company will open one more HomePro store in Johor Bahru, Malaysia, by the end of 2017. HMPRO plans to continue to add more stores in Thailand and Malaysia.

HMPRO generally introduces new store formats to capture new market segments. Recently, it introduced a new store format called "HomePro S". A HomePro S store is a small store, located in a shopping mall, with a store area ranging from 1,200-1,500 sq.m. A HomePro S store is designed under the "small, selected, and service" concepts to serve urban customers and condominium residents with variety of home-related products that match a metropolitan lifestyle. A HomePro S store still offers service just like the original format, a HomePro store.

HMPRO's profitability has outperformed peers and is gradually widening. HMPRO's margin of earnings before interest, tax, depreciation and amortization to total sales or EBITDA margin is high, ranging from 14.3%-15.1% in 2014-2016. Most peer companies showed an EBITDA margin at around 8%-9% over the same period. Also, HMPRO's profitability has been improving since 2015. EBITDA margin (adjusted with lease obligation) improved from 14.8% in 2014 to 15% in 2015, 15.4% in 2016, and 15.8% for the first nine months of 2017. Higher profitability was the result of a change in HMPRO's product mix, higher margins from selling private brands, and efficient control of costs. TRIS Rating believes these efforts will continue to yield benefits for the company.

The current economic slowdown and prolonged slump in the prices of agricultural products hurt same store sales of most home improvement retailers, including HMPRO. HMPRO's same-store sales grew by 1.1% year-on-year (y-o-y) in 2016, but declined to -2.5% and -6.3% in the first and second quarter of 2017 respectively. However, consumer spending showed signs of improvement in some areas of the nation in the third quarter of 2017. HMPRO's same-store sales improved modestly, growing by 2.8% y-o-y in the third quarter of 2017.

HMPRO has an extensive track record of increasing earnings. Total sales rose from Bt34,542 million in 2012 to Bt52,513 million in 2015, a compound annual growth rate (CAGR) of 15%. Funds from operations (FFO) grew at a 17% CAGR. However, after 2015, the sluggish economy has derailed the growth rate in sales. Sales grew at a single digit rate in 2016 and in the first nine months of 2017 despite HMPRO opening more stores. Sales inched up 8.4% y-o-y to Bt56,928 million in 2016 and then increased to Bt44,171 million, a 5% y-o-y rise in the first nine months of 2017. The growth rate in sales has slowed, but HMPRO is focusing on enhancing its operating efficiencies and improving the product mix to boost profitability. As a result, FFO increased satisfactorily, rising by 14.1% y-o-y to Bt7,297 million in 2016 and 13.2% y-o-y to Bt5,802 million for the first nine months of 2017.

The company made Bt5,143 million in capital expenditures in 2016, compared with Bt5,000-Bt7,000 million per year previously. These investments were sufficiently funded by cash flow from operations. Capital spending for the first nine months of 2017 was merely Bt1,221 million, 56.4% lower from the same period in 2016. The drop came because of a fall in new store openings in Thailand. However, the company paid generous cash dividends during 2016 through the first nine months of 2017. As a result, the total debt to capitalization ratio (including operating lease obligations) was relatively flat at 51.1% at the end of September 2017, from 49.3% in 2015. Cash flow protection remained sound. The FFO to total debt ratio was 39% in 2015, 38.6% in 2016, and 44.8% (annualized, from the trailing 12 months) for the first nine months of 2017. The EBITDA interest coverage ratio has stayed healthy, ranging from 11.3-13.7 times during 2015 through the first nine months of 2017.

TRIS Rating's base-case scenario assumes the private sector consumption will gradually recover as the economy revives. The company plans to add at least six stores per year. Including maintenance capital expenditures and the investment in a new automatic distribution center, capital expenditures are budgeted at about Bt2,500-Bt4,500 million per year. TRIS Rating forecasts HMPRO's revenues will be rising from Bt60,000 million in 2017 to Bt75,000 million by 2020. FFO will rise accordingly from Bt7,500 million to Bt9,500 million over the next few years. The debt to capitalization ratio is projected to stay around 50% and the FFO to total debt ratio will improve to more than 45%.

Rating Outlook

The "positive" outlook reflects the expectation that HMPRO's profitability and cash flow will continue to improve. HMPRO's rating could be upgraded, should its cash flow generation enlarge as expected while capital structure and cash flow protection measures are well maintained. On the contrary, the outlook could be revised downward if the financial performance is weaker than expected or if leverage is significantly higher, either from an aggressive expansion or from the poorer operating performance.

Home Product Center PLC (HMPRO)

Company Rating:	A+
Rating Outlook:	Positive

Financial Statistics and Key Financial Ratios*

Unit: Bt million

	Jan-Sep 2017	2016	2015	2014	2013	2012
		------------------------- Year Ended 31 December------------------------				
Sales	44,171	56,928	52,513	47,965	40,112	34,542
Gross interest expense	349	504	544	466	277	146
Net income from operations	3,356	4,196	3,508	3,313	3,068	2,679
Funds from operations (FFO)	5,802	7,297	6,394	5,623	4,884	3,993
Total capital expenditures	1,221	5,143	4,807	7,068	9,669	5,688
Total assets	49,134	51,746	46,991	44,313	35,942	25,868
Total debt	15,463	16,875	14,377	13,876	9,787	5,523
Shareholders' equity	17,113	17,490	16,903	15,702	12,716	9,927
Operating income before depreciation and amortization as % of sales**	15.81	15.42	15.01	14.80	14.91	14.51
Pretax return on permanent capital (%)	13.26 ***	16.93	16.04	17.36	21.01	25.51
Earnings before interest, tax, depreciation, and amortization (EBITDA) interest coverage (times)	13.74	13.12	11.34	11.76	14.49	17.92
FFO/total debt (%)	44.82 ***	38.56	38.95	35.00	42.06	54.60
Total debt/capitalization (%)	51.08	52.06	49.34	50.68	47.80	42.42

*	*Consolidated financial statements*
**	*Including other recurring income*
***	*Annualized with trailing 12 months*
Note:	*All are operating leased adjusted ratios*

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