

MUD & HOUND PLC

No. 45/2022
29 March 2022

CORPORATES

Company Rating: BBB-
Outlook: Negative

Last Review Date: 22/03/21

Company Rating History:

Date	Rating	Outlook/Alert
21/04/20	BBB-	Negative
11/05/17	BBB-	Stable

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RATIONALE

TRIS Rating affirms the company rating on Mud & Hound PLC (MUD), formerly known as Mudman PLC (MM), at “BBB-” with a “negative” outlook. The company rating incorporates MUD’s stand-alone credit profile (SACP) of “bb+” and our assessment of MUD’s status as a “core subsidiary” of Sub Sri Thai PLC (SST, rated “BBB-/Negative” by TRIS Rating).

The company rating on MUD continues to reflect MUD’s market position in the highly competitive and fragmented chain restaurant and quick service restaurant (QSR) business. The rating is weighed down by MUD’s elevated financial leverage due to continued investment for expansion amid depressed earnings brought about by the prolonged Coronavirus Disease 2019 (COVID-19) pandemic. The negative outlook reflects our concerns over the company’s planned investment for expansion in the restaurant business coupled with uncertainty surrounding the COVID-19 situation which could heighten the company’s debt level and financial leverage.

KEY RATING CONSIDERATIONS

Continued pressure in the restaurant segment due to prolonged pandemic

MUD’s operating performance recovered slower than we previously expected due to the prolonged COVID-19 pandemic. The government implemented several measures aimed at curbing the spread of the disease together with dine-in restrictions from time to time in 2021 due to multiple surges in COVID-19 cases and the emergence of new COVID-19 variants. Among all MUD’s brands, Greyhound Café (GHC) was the hardest hit as it relies mainly on dine-in sales and its delivery efforts were not particularly successful. Au Bon Pain (ABP) was also severely affected due to the absence of tourists and the work-from-home trend. The combined sales of GHC and ABP, which accounted for about half of MUD’s total sales pre-COVID-19, were 53% below the pre-COVID-19 figure. However, revenue from Dunkin’ in 2021 recovered to the pre-COVID-19 level thanks to outlet expansion. Dunkin’ has shifted its expansion strategy to focus on opening smaller kiosks in gas stations and hypermarkets. The kiosk format requires lower investment per outlet and provides more flexibility to relocate. Locations in gas stations and hypermarkets are also less affected by COVID-19 restrictions. MUD’s restaurants in France and the UK started to pick up in 2021 as both countries relaxed their COVID-19 rules. However, these restaurants did not fully recover in 2021 as there were several surges in infection cases throughout the year.

MUD’s revenue remained flat year-on-year (y-o-y) at THB2.3 billion in 2021, a 24% decline from the 2019 level. The company’s earnings before interest, taxes, depreciation, and amortization (EBITDA) increased by 20% y-o-y to THB425 million in 2021 thanks to cost control efforts, several rental waivers by landlords, and support from the governments of the UK and France.

Operating performance to gradually recover with pressure on profitability

We expect MUD’s operating performance to gradually recover as the COVID-19 situation improves. Under our base-case forecast, we expect MUD’s revenue to range upward from THB2.9-THB3.6 billion per annum in 2022-2024. We expect the COVID-19 restrictions to be more relaxed than last year as Thailand and many parts of the world have achieved high vaccination rates and vaccines have proved effective in preventing severe illness and death.

We anticipate more pressure on MUD's profitability due to intense competition and rising costs. MUD's EBITDA margin is expected to hover around 15% over the forecast period, compared with 18% in 2021, which translates into EBITDA of THB440-THB570 million per annum during 2022-2024. We view that restaurant operators may need to keep offering sales promotions and spend more on marketing activities to stay competitive. We also view the rising popularity of delivery platforms as a threat to MUD as competition further intensifies while MUD's presence on delivery channels is limited. Besides, the Russia-Ukraine war has pushed up utility costs, transportation costs, and the prices of raw materials significantly, especially the price of wheat flour which is one of the major raw materials of Dunkin' and Au Bon Pain. MUD is expected to be impacted moderately as the company has secured the price of wheat flour for the first half of 2022. However, rising prices could further pressure MUD's profitability if the ongoing geopolitical conflicts are protracted.

Overseas growth plan interrupted by COVID-19

As part of an effort to diversify internationally, the company in late 2017 acquired a well-known French restaurant, "Le Grand Vefour", in Paris. In the same period, the company opened its first owned GHC restaurant outside of Thailand in London. However, the performance of both restaurants fell short of expectations pre-COVID-19 and worsened during the pandemic. In addition, the company, together with business partner, Mr. Guy Martin, the head chef of Le Grand Vefour, opened another four restaurants in Paris, namely, "Pasco", "Augustin", and "A-Noste" in 2020, and "La Mere Lachaise" in early 2022.

We hold the view that the overseas expansion adds uncertainty to the company's business risk profile as the operating environments of the restaurant industry vary widely from country to country, while the headwinds caused by the pandemic are also intensifying the challenges. However, if the overseas expansion is successful, it will provide the company with more diversified sources of revenue and better opportunities for growth.

Elevated financial leverage

MUD's financial leverage fell y-o-y but remained elevated in 2021 due to depressed earnings brought on by the prolonged COVID-19 pandemic and the company's continued investment in outlet expansion. The company's debt to EBITDA ratio fell to 4.5 times in 2021, compared with 5.1 times in 2020. Under our base-case forecast, we expect MUD's debt to EBITDA ratio to edge up to 4.7 times in 2022 due to expected high capital spendings, before gradually improving to 4 times in 2024 as its earnings recover to pre-COVID-19 levels. We expect capital expenditure of around THB200 million in 2022, and around THB230 million in total in 2023-2024. We expect the capital spendings to be used mainly for outlet expansion, especially for the Dunkin' brand.

As of December 2021, MUD had consolidated debt of THB1.3 billion, of which around THB1.0 billion was considered priority debt. MUD's priority debt comprised secured loans and debentures at the parent company and secured and unsecured loans at subsidiaries. As its priority debt ratio was 80%, higher than the threshold of 50% according to TRIS Rating's "Issue Rating Criteria", we view that MUD's senior unsecured creditors could be significantly disadvantaged to its priority debt holders with respect to claims against the company's assets.

MUD's debentures have a key financial covenant that requires the company to maintain its interest-bearing debt to equity ratio below 3 times. As of December 2021, the ratio was 0.53 times. The company's long-term bank loan also has key financial covenants that require the company to maintain the total liabilities to equity ratio below 2 times, the debt service coverage ratio above 1.2 times, and the net debt to EBITDA ratio below 3 times. As of December 2021, the ratios were 1.32 times, 0.79 times, and 4.41 times, respectively. The company received a waiver from lenders on the debt service ratio and debt to EBITDA ratio thresholds for 2021. We view that the company may breach the covenants and need to seek waivers again in 2022 should its performance recover in line with or below expectations.

Tight liquidity

We assess MUD's liquidity to be tight during the next 12 months. The company's sources of funds comprised cash and cash equivalents of around THB200 million as of December 2021, projected funds from operations (FFO) of around THB340 million, and available credit lines of around THB30 million. The company's uses of funds include debt repayments of around THB400 million, lease obligations of around THB200 million, and expected capital expenditures of THB200 million. MUD may need to refinance a major portion of its debts coming due and secure additional funding to meet its investment plan.

BASE-CASE ASSUMPTIONS

- Revenue to range upward from THB2.9-THB3.6 billion annually during 2022-2024.
- EBITDA of THB440 million in 2022 and THB530-THB570 million per annum during 2023-2024.
- Capital spending to be around THB200 million in 2022 and THB230 million in total during 2023-2024.

RATING OUTLOOK

The “negative” outlook reflects our concern over the company’s planned investment for expansion in the restaurant business coupled with uncertainty surrounding the COVID-19 situation which could heighten the company’s debt level and financial leverage beyond our expectations.

RATING SENSITIVITIES

Any change in SST’s credit profile or a change in our assessment of MUD’s core status within the SST group could affect the company rating on MUD.

We could revise the SACP on MUD downward if its credit metrics turn out to be weaker than our expectations, either from the prolonged negative impact of COVID-19 or aggressive debt-funded investments. On the other hand, we could revise the SACP on MUD upward if the company’s operating performance demonstrates signs of sustainable recovery such that the credit metric outperforms or tracks our base-case projection.

A change in SACP on MUD does not necessarily translate into a change in the company rating. However, as MUD is a key contributor to SST, a change in SACP on MUD could potentially lead to a corresponding change in SST’s credit profile, thereby leading to a change in the company rating on MUD.

COMPANY OVERVIEW

MUD was established in 2006 and listed on the Market for Alternative Investment (MAI) on 11 April 2017. As of December 2021, SST, a warehouse and document storage service provider, was the major shareholder, owning 66% of MUD’s paid-up shares. The company has two lines of business: food and beverages and fashion apparel. The company is the master franchisee of the “Dunkin’ Donuts”, “Au Bon Pain”, and “Baskin Robbins” brands in Thailand. In 2014, the company expanded to the full-service restaurant segment by acquiring the Greyhound Group, which owns and operates the GHC chain and also produces and distributes fashion and lifestyle products under the Greyhound brand. MUD also operates a hospital food court under the “M-Kitchen” brand and provides in-patient food services in a private hospital. Additionally, MUD has five restaurants in France including Le Grand Vefour, Pasco, Augustin, A-Noste, and La Mere Lachaise.

KEY OPERATING PERFORMANCE

Table 1: Sales Contribution

Business Line	2018		2019		2020		2021	
	Million THB	%						
Dunkin' Donuts	1,048	34	957	33	873	40	1,013	47
Au Bon Pain	683	22	621	21	401	19	333	15
Baskin Robbins	108	3	101	3	63	3	51	2
Greyhound Cafe	947*	31	944*	32	579*	27	405*	19
Greyhound Fashion and Lifestyle	150	5	147	5	149	7	165	8
Le Grand Vefour	137	4	131	5	43	2	103	5
Others	22	1	20	1	59	2	98	4
Eliminations	-13	0	-8	0	-1	0	-2	0
Total sales	3,082	100	2,913	100	2,166	100	2,166	100

* Including GHC London

Source: MUD

Table 2: Number of Outlets

Food Outlets	Outlet Number	Type of Restaurant
Dunkin' Donuts	419	QSR
Au Bon Pain	67	QSR
Baskin Robbins	26	QSR
Greyhound Café	27*	Full service restaurant
Greyhound Café (franchised)	14	Full service restaurant
Le Grand Vefour	1	French restaurant
Pasco	1	French restaurant
Augustin	1	French restaurant
A-Noste	1	Tapas restaurant
La Mere Lachaise	1	French restaurant
Total outlets	558	

* Including GHC London

Source: MUD

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS

Unit: Mil. THB

	-----Year Ended 31 December -----				
	2021	2020	2019	2018	2017
Total operating revenues	2,316	2,316	3,060	3,233	2,962
Earnings before interest and taxes (EBIT)	(17)	(147)	64	75	36
Earnings before interest, taxes, depreciation, and amortization (EBITDA)	425	354	552	523	510
Funds from operations (FFO)	321	266	449	423	409
Adjusted interest expense	99	85	89	81	80
Capital expenditures	233	245	154	174	266
Total assets	4,897	4,792	4,210	4,301	4,338
Adjusted debt	1,925	1,796	1,470	1,355	1,152
Adjusted equity	2,110	2,236	2,696	2,788	2,845
Adjusted Ratios					
EBITDA margin (%)	18.33	15.28	18.03	16.18	17.23
Pretax return on permanent capital (%)	(0.40)	(3.46)	1.48	1.75	0.91
EBITDA interest coverage (times)	4.29	4.14	6.22	6.49	6.37
Debt to EBITDA (times)	4.53	5.07	2.67	2.59	2.26
FFO to debt (%)	16.66	14.84	30.51	31.22	35.48
Debt to capitalization (%)	47.70	44.54	35.29	32.70	28.82

RELATED CRITERIA

- Key Financial Ratio and Adjustments for Corporate Issuers, 11 January 2022
- Issue Rating Criteria, 15 June 2021
- Group Rating Methodology, 13 January 2021
- Rating Methodology – Corporate, 26 July 2019

Mud & Hound PLC (MUD)

Company Rating:	BBB-
Rating Outlook:	Negative

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