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PRE-BUILT PLC

CORPORATES

Company Rating:	BBB
Outlook:	Stable

Last Review Date: 08/03/19

Company Rating History:

Date	Rating	Outlook/Alert
11/04/17	BBB	Stable
30/06/14	BBB-	Stable

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RATIONALE

TRIS Rating affirms the company rating on Pre-Built PLC (PREB) at "BBB" with a "stable" rating outlook. The rating reflects the company's well-built track record in the construction of high-rise buildings, robust profitability, and adequate liquidity. Conversely, these strengths are weighed down by the high concentration risk in the end-markets PREB serves and the grim outlook for domestic residential construction. The rating also takes into account a potential rise in leverage and execution risk following the company's strategic move into the property development business.

KEY RATING CONSIDERATIONS

Well-established market presence

PREB's business profile is acceptable, backed by its highly regarded track record. PREB is best known for the construction of high-rise buildings in a number of end-use segments, such as residential properties, condominiums, commercial properties, hotels, and industrial projects. The company also has good reputation in completing construction projects as planned.

PREB constructs condominium projects chiefly in Bangkok and in prime locations outside the metropolitan areas. PREB's customer base largely comprises reputable property developers, most of which are listed on the Stock Exchange of Thailand (SET).

Over the past five years, PREB has secured new contracts worth Bt3.5-Bt5.5 billion per year. In the first nine months of 2019, PREB mustered Bt4.1 billion in new contracts.

Continued discipline to keep profitability strong

PREB has maintained long-standing discipline in its business conduct to ensure continued profits. The company generally avoids price-matching strategies to lure new construction contracts to scale up revenue. Instead, the company is cost-conscious and selective. PREB focuses mostly on projects which are viable and potentially lucrative.

PREB uses pre-cast concrete system technology in its building projects. By using this technology, PREB can control construction costs and project timelines, the two crucial factors for success. PREB's gross margin for construction is generally in the 12%-15% range, a relatively higher level than most SET-listed contractors.

PREB's operating performance in the first nine months of 2019 was in line with TRIS Rating's forecast, albeit with lower-than-expected revenues. Revenue was Bt3.1 billion, down 2% year-over-year. However, its gross margin remained high at 14.4%. Earnings before interest, tax, depreciation, and amortization (EBITDA) came in at Bt304 million.

High concentration risk remains

PREB's strengths are weighed down by its high reliance on construction of condominiums for a small number of clients. Over the past three years, the biggest client has been Ananda Development PLC (ANAN). On average, ANAN's condominium projects have contributed about 25% of PREB's revenue each year.

At the end of September 2019, PREB's backlog stood at Bt9.5 billion. Its biggest clients were ANAN and Origin Property PLC (ORI). Projects for these two large clients made up about 60% of the value of PREB's project backlog. This level of customer concentration risk keeps a lid on the rating. However, the risk is somewhat alleviated as the major customers are creditworthy. Payment risk is acceptable.

The rating is also constrained by the cyclical nature of the engineering and construction (E&C) industry. The industry cycles are influenced by the property market. Prolonged dismal performance in the property market could undermine the sustainability of the company's revenue streams. Stiff competition in the E&C industry also poses a downside risk.

Re-entering property development

PREB re-entered the property development business after the divestiture of its previously-owned flagship property company a few years ago, in a bid to uplift both revenue and profitability. Through joint ventures (JV) with other property developers, PREB is now developing residential projects with a combined value of Bt6.6 billion. Ongoing JV projects comprise three townhomes and three condominiums. Added to that, PREB has developed four wholly-owned residential projects, comprising two condominiums in prime locations of Bangkok and two single-detached house (SDH) projects in outer Bangkok. These projects are valued at Bt5.2 billon.

Given its lesser-known brand, TRIS Rating holds the view that PREB would need to offer more compelling products to customers, potentially by offering more competitive prices. With the backdrop of fierce market competition, PREB could be hurt by slow-selling properties.

Sluggish residential property market is the key downside risk

In our view, the key downward pressure for PREB is the sluggish demand for residential properties, caused by several factors, including a slowdown in the economy, weakened purchasing power among local and foreign buyers, and high levels of household debt. Further, we expect adverse impacts after the new loan-to-value (LTV) measures implemented by the Bank of Thailand take full effect. As a result, new project launches in 2019 of rated property developers dropped by 20% from 2018. In particular, launches of condominium projects dropped by 40%. We view any recovery of the property market as being far off.

The dismal property market could have serious repercussions on PREB's operating performance for a number of reasons. Firstly, PREB's major clients are property developers enduring the current market sluggishness. Secondly, PREB's construction business is concentrated in condominium projects. Further, the current glut of residential properties and markdowns could negatively impact PREB's property sales.

In effect, we expect that PREB will slow down growth in its property business. PREB is expected to put off developing several projects in the pipeline until the market recovers. The company's previous plans to develop new projects and acquire new land plots should also been put on hold for the years ahead. As a result, we expect the revenue contribution from PREB's property development business will remain small in the next three years, considering the number of ongoing projects.

Profitability expected to contract

In our base case for 2020-2022, we expect PREB's total revenue will be in the range of Bt5-Bt6 billion per year, most of which will be derived from the construction business. We expect PREB will maintain good operating performance, given its efficient cost control and its strategy to focus on high-margin construction works. Nonetheless, the company's profitability will likely soften in the next three years due to intensifying competition in the construction business and the slowdown in the property development sector.

Our forecast assumes the overall gross profit margin will stay at 12%-13%, compared with 14%-18% over the past three years. EBITDA will likely be Bt350-Bt400 million per year while funds from operations (FFO) are expected to stay in the range of Bt250-Bt300 million per year.

Financial leverage is on the rise but acceptable

TRIS Rating holds the view that PREB's leverage will likely rise in the next few years to support its property business. We expect PREB's debt to capitalization ratio to stay in the 30%-35% range. The expected leverage level is relatively lower than our previous forecast of around 50%-55%, as we expect that PREB will materially cut down its foregoing investment plans. As for cash flow protection, the ratio of debt to EBITDA should stay at around 3 times over the next three years.

In assessing the company's financial leverage, TRIS Rating includes the debt of associated companies proportionate to PREB's respective guarantee obligations to mirror the company's potential indebtedness. In TRIS Rating's base-case forecast, adjusted debt could increase to around Bt2-Bt2.5 billion over the next three years from Bt1.5 billion as of September 2019.

Adequate liquidity

We assess PREB to have adequate liquidity over the next 12 months. As of September 2019, cash and short-term investments amounted to Bt883 million. FFO over the next 12 months are forecast at around Bt250 million. As of September 2019, PREB had Bt711 million in short-term loans for land purchases coming due over the next 12 months. The company plans to convert its short-term loans to long-term project loans thereafter. Over the next three years, we forecast the ratio of FFO to debt will stay above 20%, while the EBITDA interest coverage ratio is expected to stay above 6 times.

According to the key financial covenants of bank loans, PREB has to maintain its total liability to equity ratio below 2.5 times. The ratio at the end of September 2019 was 1.6 times.

BASE-CASE ASSUMPTIONS

- Revenue will be in the Bt5-Bt6 billion per year range during 2019-2022.
- Gross profit margin will stay in the range of 11%-13%.
- Operating margin (operating income before depreciation and amortization as a percentage of sales) will be 6%-7% over the next three years.
- Potential new contracts for construction projects to be around Bt3.5 billion per year.
- Residential property project launches to be worth Bt1.8 billion in 2020 and Bt700-Bt800 million in 2021.
- Construction material sales will be in the range of Bt500-Bt550 million per year.

RATING OUTLOOK

The “stable” rating outlook reflects TRIS Rating’s expectation that PREB will sustain its competitive edge in its core construction business. PREB’s operating performance will meet our expectations. We also expect PREB will continue to avoid unnecessary debt load amidst a sluggish property market. Despite a potential surge in debt to support ongoing projects, we expect its leverage and cash flow protection to stay at the projected levels.

RATING SENSITIVITIES

A rating upgrade is unlikely in the near term. However, it could materialize if PREB significantly enhances revenue and profitability from the current levels for a sustained period while its leverage remains at a prudent level.

In contrast, the rating and/or outlook could be lowered if PREB loses its competitiveness and its profitability drastically declines for a sustained period. Downward rating pressure could develop in a scenario of aggressive investments in residential property projects, which considerably deteriorate capital structure and cash flow protection. For instance, should the debt to EBITDA ratio exceed 5 times on a sustained basis.

COMPANY OVERVIEW

PREB was established in 1995 by the Charoentra family, AP (Thailand) PLC (AP), and the Quest Capital Group. The company is a general contractor focusing on the construction of high-rise buildings for private sector clients. PREB was listed on the SET in 2005. As of November 2019, the founding Charoentra family was the company’s largest group of shareholders, owning 26.3% of the total number of shares.

PREB also has the capability to build industrial plants and public works (infrastructure projects) as well as take on system and design work. However, the company remains focused on the construction of residential property projects. PREB’s customer base largely comprises reputable property developers, most of which are listed on the SET.

PREB expanded into the production and distribution of construction materials in 2004, through a wholly-owned subsidiary, PCM Construction Material Co., Ltd. (PCM), under the “PCM” brand. PCM produces precast concrete. In 2009, PREB established a wholly-owned subsidiary, Built Land Co., Ltd., to develop residential property including condominium and townhouse projects. PREB’s expansion into the property development segment was a strategic move aimed at ramping up revenue and profitability.

In 2017, PREB made a significant change in strategy by divesting Built Land for around Bt900 million. PREB recorded a gain of Bt289 million from the divestiture, leaving the company with a debt-free balance sheet and a considerable amount of cash.

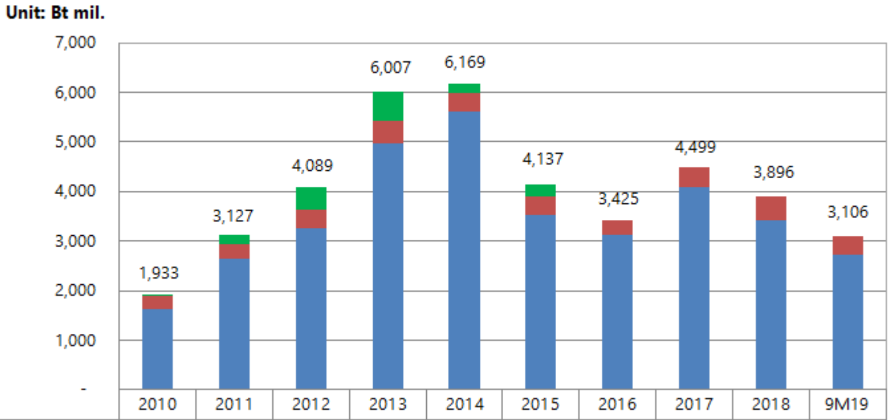
PREB re-entered the property development business in March 2017 with the establishment of Pre-Built Holding Co., Ltd. (PBH), a wholly-owned investment vehicle. PBH develops residential property projects through JVs with other property developers. PBH started developing residential property projects in mid-2017. In the meantime, PREB has set up IS Am Are

Co., Ltd. (IAA) to develop its own property projects. IAA's current projects comprise two condominium projects in the Sukhumvit area, and two SDH projects, with a combined value of around Bt5.2 billion.

The construction segment has contributed more than 85% of PREB's total revenue over the past five years.

KEY OPERATING PERFORMANCE

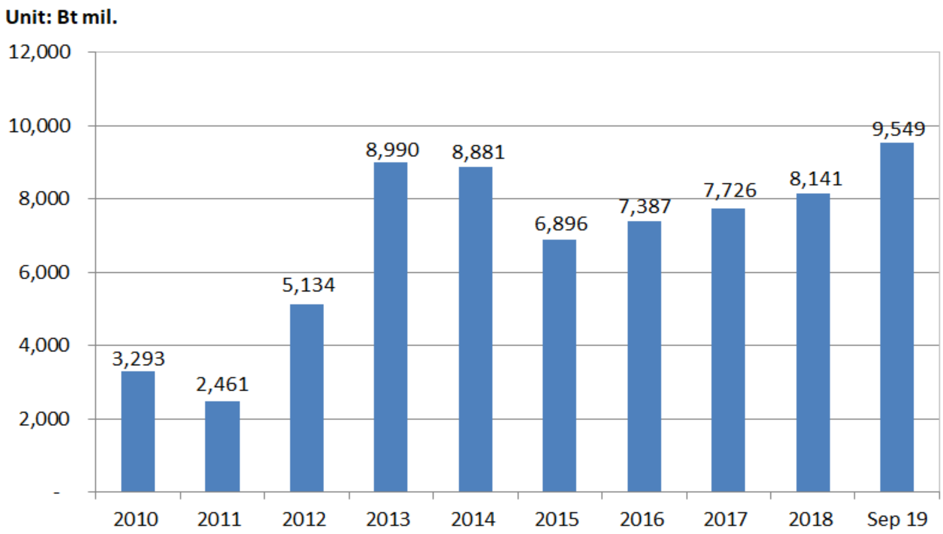
Chart 1: Revenue Breakdown



	2010	2011	2012	2013	2014	2015	2016	2017	2018	9M19
Residential property	30	192	462	577	194	234	0	0	0	0
Sales of construction materials	285	290	371	451	357	366	309	408	469	384
Construction	1,618	2,645	3,256	4,979	5,618	3,538	3,117	4,091	3,427	2,721

Source: PREB
Note: Restated in 2016 and 2017

Chart 2: Backlog as of Sep 2019



Source: PREB

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS*

Unit: Bt million

	Jan-Sep 2019	-------------Year Ended 31 December ----------- 2018	2017	2016	2015
Total operating revenues	3,112	3,903	4,505	3,444	4,158
Earnings before interest and taxes (EBIT)	274	477	428	352	381
Earnings before interest, taxes, depreciation, and amortization (EBITDA)	304	510	472	403	433
Funds from operations (FFO)	206	407	257	236	320
Adjusted interest expense	41	6	5	43	28
Capital expenditures	34	55	17	26	21
Total assets	5,660	5,030	4,326	5,056	5,253
Adjusted debt	1,496	587	0	0	0
Adjusted equity	2,212	2,264	2,128	2,040	1,409
Adjusted Ratios					
EBITDA margin (%)	9.76	13.07	10.47	11.69	10.41
Pretax return on permanent capital (%)	8.84 **	15.79	18.43	15.41	18.59
EBITDA interest coverage (times)	7.39	84.14	101.84	9.28	15.72
Debt to EBITDA (times)	3.97 **	1.15	0.00	0.00	0.00
FFO to debt (%)	17.46 **	69.37	n.a.	n.a.	n.a.
Debt to capitalization (%)	40.34	20.60	0.00	0.00	0.00

* *Consolidated financial statements*
** *Annualized with trailing 12 months*
n.a. *Not available*

RELATED CRITERIA

- Rating Methodology – Corporate, 26 July 2019
- Key Financial Ratios and Adjustments, 5 September 2018

Pre-Built PLC (PREB)

Company Rating:	BBB
Rating Outlook:	Stable

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