

QUALITY HOUSES PLC

No. 137/2023
31 July 2023

CORPORATES

Company Rating:	A-
Issue Ratings:	
Senior unsecured	A-
Outlook:	Stable

Last Review Date: 14/02/23

Company Rating History:

Date	Rating	Outlook/Alert
26/07/22	A-	Negative
18/04/13	A-	Stable
24/11/11	A-	Negative
10/05/10	A-	Stable
02/07/09	A-	Negative
21/07/08	A-	Stable
12/07/04	BBB+	Stable
24/03/04	BBB+	-
23/07/03	BBB	-

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RATIONALE

TRIS Rating affirms the company rating on Quality Houses PLC (QH) and the ratings on QH's senior unsecured debentures at "A-". At the same time, TRIS Rating revises the company's rating outlook to "stable" from "negative". The rating outlook revision reflects QH's improved financial risk profile, which is attributed to the recovery in its revenue and earnings, as well as improving financial leverage.

The ratings continue to reflect its relatively diversified product portfolio and significant dividend income and financial flexibility derived from its investments in affiliates. However, the ratings are weighed down by the cyclical nature of the residential property industry and our concerns over the reimposition of the loan-to-value (LTV) rules and interest rate hikes which could negatively impact demand for housing in the short to medium term.

KEY RATING CONSIDERATIONS

Reviving operating performance

QH's total operating revenue in 2022 revived to THB9.2 billion, grew 14% year-on-year (y-o-y). The revenue from the residential property business and hotel operations rose by 10% y-o-y and 128% y-o-y, respectively. The gross profit margin also increased to 34% in 2022, up from the previous range of 30%-31% during 2020-2021. Looking ahead, TRIS Rating expects QH's earnings to continue improving, driven by the strong rebound of hotel operations and an improvement in profit margins from its residential projects.

Our base-case scenario projects QH's total operating revenue to hover around THB10 billion during 2023-2025, with residential sales contributing around 90% of the total revenues. The company's gross profit margin is expected to remain stable within the 32%-33% range. Furthermore, we project QH's earnings before interest, taxes, depreciation, and amortization (EBITDA) to exceed THB3 billion, and the EBITDA margin to fall within the 29%-31% range over the forecast period.

Minimal impact from the expiration of leasehold contracts

Regarding QH's hotel operations, it is anticipated that the occupancy and room rates should revert to the pre-pandemic levels this year. The average occupancy rate is expected to reach 70% with the average room rate around THB2,900 per night. However, QH's annual rental and service income could decline slightly in 2025 onwards since leasehold contracts for Centre Point Hotel Silom and Q-House Sathorn will expire by July 2023 and December 2023, respectively. The company decided to extend only one-year leasehold contract for Centre Point Hotel Silom while Q-House Sathorn is under lease extension negotiation.

It is expected that Centre Point Hotel Silom will be acquired by Quality Houses Hotel and Residence Freehold and Leasehold Property Fund (QHHR) after converting into real estate investment trusts (REITs) in the beginning of 2025. QH plans to lease back Centre Point Hotel Silom from QHHR. We expect its rental and service income should be minimal changed. Profitability in hotel operations will likely be affected by the leaseback condition, resulting in the gross profit margin for the rental and service business softening in 2025 from the 41%-42% range in 2023-2024.

Relatively diversified product portfolio

In our view, QH's product portfolio is relatively diversified. QH's portfolio comprises single-detached houses (SDH), semi-detached houses (semi-DHs), townhouses, and condominiums, covering almost all of the segments in the residential property market. The company captures the high-end SDH segment with selling prices above THB20 million per unit under the "Pruekpirom" brand, the middle- to high-end SDH segment with unit prices of THB10-THB20 million under the "Laddarom" brand, middle SDH and semi-DH with units priced between THB5-THB12 million under the "Vararom" and "Casa Ville" brands, and affordably priced semi-DH and townhouses with selling prices between THB2.5-THB6 million per unit under the "Q District" brand.

As of March 2023, QH had 54 landed property projects and 12 condominium projects, with total remaining project value of THB38.8 billion (including built and un-built units). Of the unsold value, 71% was made up of landed property projects while ready-to-transfer condominium projects made up the remainder.

Considerable dividend contribution from investments in affiliates

QH's sizeable portfolio of marketable securities helps enhance its liquidity and financial flexibility. QH holds stakes in two listed companies and two property funds: Home Product Center PLC (HMPRO, a 19.9% stake), LH Financial Group PLC (LHFG, 13.7%), QHPF (25.7%), and QHHR (31.3%). These four entities grant dividends to QH on a recurring basis. Over the past five years, QH recognized share of profits from its investments of THB1.4-THB1.9 billion per annum and received dividends of THB1.1-THB1.5 billion per annum. We expect QH to receive dividends from its investments around THB1 billion per annum over the forecast period.

In addition, the market value of these investments is substantial. At the end of March 2023, the portfolio carried a fair value of THB42.6 billion. The investment in these affiliates reinforces the financial flexibility of the company and the divestment of the affiliates would strengthen QH's financial profile significantly.

Leverage remains low

We expect QH's debt to capitalization ratio to stay in the 25%-28% range and the debt to EBITDA ratio to hover around 3.5 times over the next three years. QH's plan to accelerate the sales of housing units in its existing projects and focus mainly on the launches of landed property projects should help keep its leverage low. QH plans to launch new landed property projects worth around THB10 billion per annum. The budget for land acquisition is expected to be around THB2.5-THB3 billion per year.

At the end of March 2023, QH had total consolidated debts of THB11.3 billion, comprising THB8.5 billion debentures, THB2.6 billion long-term loans, and THB200 million short-term loans from financial institutions. THB1.1 billion of its total debts were considered priority debts, which translates to a priority debt to total consolidated debt ratio of 10%.

Adequate liquidity

We assess QH to have adequate liquidity to cover its debt repayments over the next 12 months. As of March 2023, the company has debts of THB5.1 billion coming due in the next 12 months, comprising THB3 billion debentures, THB1.9 billion term loan repayments, and THB200 million short-term loans from financial institutions. The company plans to refinance maturing debentures with the new issuance of debentures and long-term loans.

QH's sources of liquidity included cash on hand of THB1.5 billion and available short-term credit facilities of around THB4 billion. We forecast QH's funds from operations (FFO) over the next 12 months to be around THB2 billion. The company also has unencumbered land at book value worth THB5.3 billion, which can be pledged as collateral for new credit facilities.

The financial covenant on QH's bonds and bank loans require the company to maintain its net interest-bearing debt to equity ratio below 2 times. The ratio at the end of March 2023 was 0.4 times. We believe the company should have no problems complying with the financial covenant over the next 12 months.

Negative impact from reimposition of LTV rules and interest rate hikes

The reimposition of LTV rules and rising interest rates could dampen housing demand in the short to medium term. From January 2023, banks need to cap LTV at 80%-90% for second mortgage contracts and at 70% for third mortgage contracts. In our view, the LTV rules will generally have greater impact on the mid- to high-end housing segments since these buyers may have more than one mortgage contract. The impact of LTV measures to QH is partly alleviated by its well-balanced portfolio across price ranges.

On the other hand, rising interest rates will have greater impact on the debt servicing capacity of homebuyers, especially those in the lower-income segment. Interest rate hikes will also affect the funding costs of developers. However, given the easing pressure from both foreign exchange and inflation, we expect the Bank of Thailand (BOT) to raise the policy rate by

only 3-4 times this year. The BOT has already raised the policy rate in May 2023 by 25 basis points (bps) for a third consecutive time.

BASE-CASE ASSUMPTIONS

These are the key assumptions in TRIS Rating's base-case forecast for QH's operations during 2023-2025:

- QH to launch new landed property projects worth around THB10 billion per annum.
- Budget for land acquisition of THB2.5-THB3 billion per annum.
- Total operating revenue in the range of THB9.5-THB10 billion per annum.
- Gross profit margin to hover around 33% and the EBITDA margin to wane to 29%-31%.

RATING OUTLOOK

The "stable" outlook reflects our expectation that QH should be able to deliver operating performance in line with our forecast and maintain its financial profile at the current level. We expect QH to generate revenues of THB9.5-THB10 billion per annum and the EBITDA should stand above THB3 billion over the forecast period. The company should maintain the debt to capitalization ratio below 50% and the debt to EBITDA below 5 times during 2023-2025.

RATING SENSITIVITIES

The ratings and/or outlook could be revised downward should the company's operating results and/or financial profile deteriorate significantly from our expectations causing the debt to capitalization ratio to reach above 50% and the debt to EBITDA ratio to exceed 5 times on a sustainable basis. A credit upside would be limited in the near term. However, a credit upside scenario could emerge if the company improves its operating performance, such that the EBITDA stay around THB5 billion with the EBITDA from its own business operations above THB3 billion on sustained basis, while its financial profile does not significantly deteriorate from the current level.

COMPANY OVERVIEW

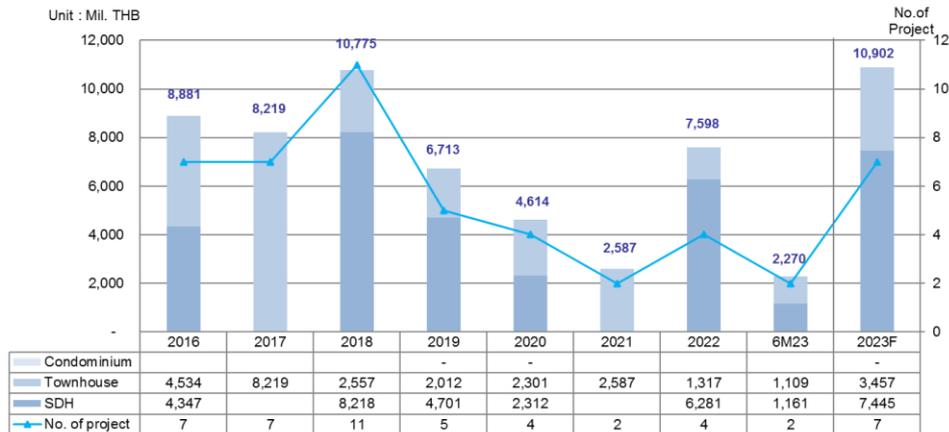
QH was established in 1983 by Land & Houses PLC (LH), the Gaysorn Group, and Dhana Siam Finance and Securities PLC. The company was listed on the Stock Exchange of Thailand (SET) in 1991. As of April 2023, LH was the largest shareholder of QH, holding a 25% stake.

QH's business profile is satisfactory. The company is one of the leading property developers in Thailand. The company offers a wide range of residential property products, including SDHs, semi-DHs, townhouses, and condominiums. QH's market position is quite strong in the housing segment priced over THB5 million per unit. Its market position in the lower-priced housing segment, where prices range between THB2.5-THB4.5 million per unit, is also acceptable. The company's housing brands are well-known and accepted by buyers.

In 1992, the company entered the residential property development segment, with a focus on high-end SDHs, under three brand names: "Pruekpirom", "Laddarom", and "Vararom". In 2006, the company introduced the Casa brand to capture the middle-income segment. In 2009, QH developed semi-prebuilt condominium projects under the "Q" and "Q House Condominium" brands. In 2010, QH introduced "The Trust" brand, which offers residential property units priced between THB1-THB3 million per unit. QH introduced the "Gusto" brand in 2012, for its THs priced at THB2-THB4 million per unit. In 2020, QH introduced the "Q Prime" brand for THs in the premium segment priced at THB6-THB7 million per unit. In 2022, QH redesigned and reshaped its product portfolio. The company intends to run its residential property business with five brand names, comprising high-end SDHs with selling prices above THB20 million per unit under the "Pruekpirom" brand, the middle- to high-end SDHs with unit prices of THB10-THB20 million under the "Laddarom" brand, middle SDHs and semi-DHs with unit prices between THB5-THB12 million under the "Vararom" and "Casa Ville" brands, and affordably priced semi-DHs and townhouses with selling prices between THB2.5-THB6 million per unit under the "Q District" brand.

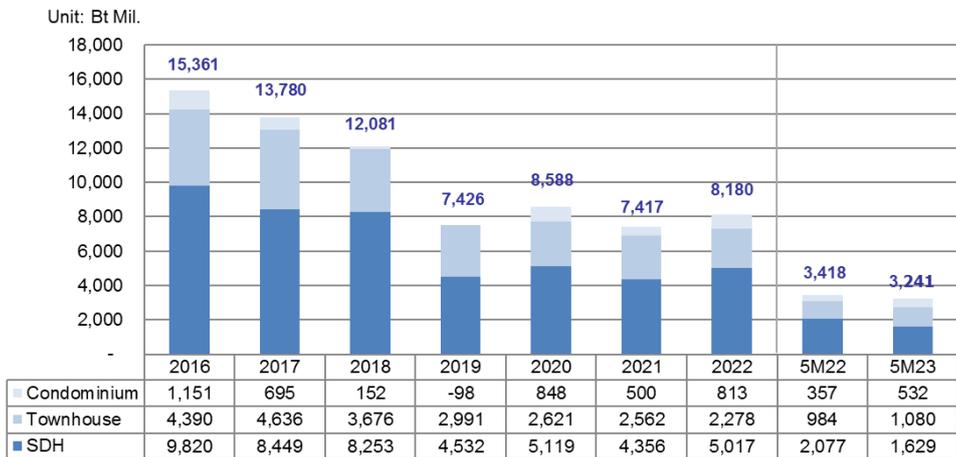
KEY OPERATING PERFORMANCE

Chart 1: New Project Launches



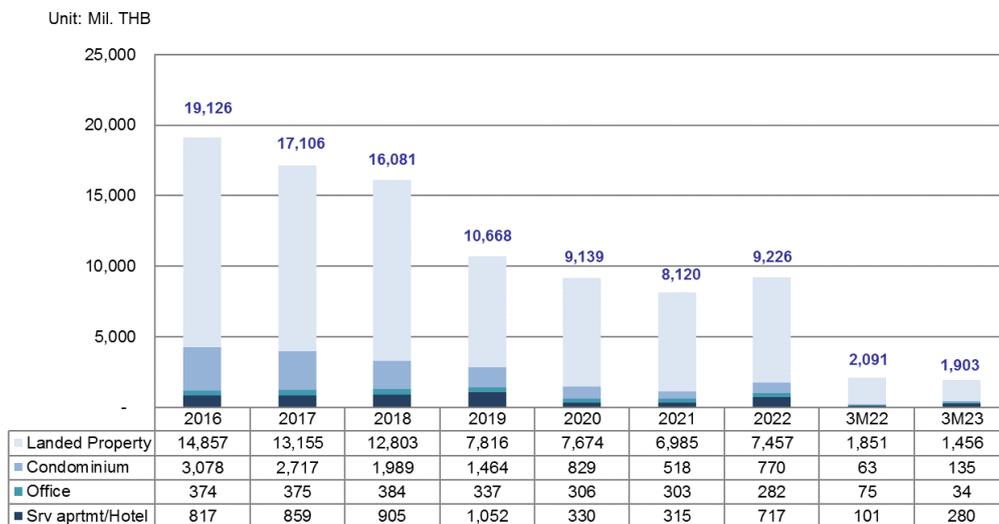
Source: QH

Chart 2: Presales Performance



Source: QH

Chart 3: Revenue from Sales and Services Breakdown



Source: QH

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS*

Unit: Mil. THB

	Jan-Mar 2023	-----Year Ended 31 December -----			
		2022	2021	2020	2019
Total operating revenues	1,903	9,226	8,120	9,138	10,680
Earnings before interest and taxes (EBIT)	736	3,185	2,460	3,086	3,871
Earnings before interest, taxes, depreciation, and amortization (EBITDA)	414	3,111	2,661	3,108	3,787
Funds from operations (FFO)	292	2,421	2,010	2,237	2,822
Adjusted interest expense	70	348	417	533	634
Real estate development investments	26,630	26,677	27,461	29,706	33,642
Total assets	43,881	43,626	46,236	47,667	50,902
Adjusted debt	10,774	11,115	13,246	15,757	18,949
Adjusted equity	28,313	27,833	26,985	26,568	26,863
Adjusted Ratios					
EBITDA margin (%)	21.75	33.72	32.77	34.01	35.46
Pretax return on permanent capital (%)	7.46 **	7.59	5.57	6.65	7.90
EBITDA interest coverage (times)	5.88	8.95	6.38	5.83	5.97
Debt to EBITDA (times)	3.56 **	3.57	4.98	5.07	5.00
FFO to debt (%)	21.91 **	21.78	15.17	14.20	14.89
Debt to capitalization (%)	27.57	28.54	32.93	37.23	41.36

* Consolidated financial statements

** Annualized with trailing 12 months

RELATED CRITERIA

- Homebuilders and Real Estate Developers Rating Methodology, 12 January 2023
- Corporate Rating Methodology, 15 July 2022
- Key Financial Ratios and Adjustments for Corporate Issuers, 11 January 2022
- Issue Rating Criteria, 15 June 2021

Quality Houses PLC (QH)

Company Rating:	A-
Issue Ratings:	
QH243A: THB3,000 million senior unsecured debentures due 2024	A-
QH246A: THB1,500 million senior unsecured debentures due 2024	A-
QH24NA: THB730 million senior unsecured debentures due 2024	A-
QH255A: THB1,000 million senior unsecured debentures due 2025	A-
QH25NA: THB720 million senior unsecured debentures due 2025	A-
QH25DA: THB550 million senior unsecured debentures due 2025	A-
QH25DB: THB1,000 million senior unsecured debentures due 2025	A-
Rating Outlook:	Stable

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