

QUALITY HOUSES PLC

No. 118/2022
26 July 2022

CORPORATES

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

Last Review Date: 20/04/22

Company Rating History:

Date	Rating	Outlook/Alert
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 "negative" from "stable". The "negative" outlook reflects a slower-than-expected recovery in QH's revenue and earnings and its weakened market position in the landed property segment. The ratings continue to reflect its diversified product portfolio, reliable dividend income from its investments in affiliates, and its prudent financial management.

The rating also incorporates our concerns over the relatively high household debt level together with the rising inflation rate which will push up development and funding costs for developers while lowering the purchasing power of homebuyers in the short to medium term.

KEY RATING CONSIDERATIONS

Lower-than-expected operating performance

QH's operating performance was weaker than TRIS Rating's previous forecast. Ongoing intense competition among property developers, a reduction of new project launches, as well as the lockdown of construction sites in Bangkok and vicinity in 2021 caused the company's residential sales further declined. In addition, the company's hospitality business was adversely affected by the lingering Coronavirus Disease 2019 (COVID-19) pandemic, which led to lower numbers of foreign tourists than expected. QH's total operating revenue in 2021 declined continuously to THB8.1 billion from more than THB15 billion in 2018, almost 10% lower than our previous target. Revenues from residential sales dropped below THB10 billion for three consecutive years.

QH's profitability also softened owing to the promotional campaigns for its slow-moving projects and depressing results from hotel operations. Its gross profit margin decreased to 30% in 2021, from 31% in 2020 and 34%-35% during 2018-2019. Furthermore, lower profit sharing from affiliates during the pandemic lessened QH's earnings base. Its earnings before interest, taxes, depreciation, and amortization (EBITDA) further declined to THB2.7 billion in 2021, from THB3.1 billion in 2020 and THB4-THB5 billion per annum in 2018-2019. Although its gross profit margin improved to 34% in the first quarter of 2022, EBITDA was only THB498 million, equivalent to 18% of our previous full-year expectation of THB2.8 billion.

Weakened market share in mid- to high-priced housing segment

Over the past few years, QH has concentrated on adjusting its products and clearing its inventory. The company launched housing projects worth only THB4.6 billion in 2020 and THB2.6 billion in 2021, a sharp decline from THB7-THB11 billion per annum during 2016-2019. The relatively slow rate of sales in its existing projects coupled with the fewer new projects has caused its market share to shrink significantly in the mid- to high-priced landed property segment, in which demand remains solid and the company used to hold a significant market share.

Looking forward, QH plans to launch more new landed property projects worth THB10 billion annually in 2022-2024 to facilitate its revenue growth. Our base-case scenario forecasts QH's total operating revenue to revive but may remain lower than THB10 billion per annum in 2022-2023. Its profitability could be

squeezed by rising development costs, intense competition from top-tier residential developers, and ongoing thin margin in hotel operations. As a result, its gross profit margin is forecast to hover around 30% with the EBITDA margin to stay in the 29%-31% range over the forecast period. A further decline in its revenues and earnings could trigger a rating downgrade.

Diversified product portfolio and relatively well-accepted brands in landed property segment

QH offers various product types comprising single-detached houses (SDH), semi-detached houses (semi-DH), townhouses (TH), and condominiums to homebuyers across diverse market segments. The company's product portfolio covers the low- to high-income segments. QH captures the high-end SDH segment with selling prices above THB25 million per unit under the brand "Pruekpirom", the middle- to high-end SDH segment with unit prices of THB15-THB25 million under the brand "Laddarom", middle SDH and semi-DH with unit priced between THB6-THB15 million under the brands "Vararom" and "Casa Ville", and affordably priced semi-DH and TH with selling prices between THB2.5-THB6 million per unit under the brand "Q District". Currently, its housing segment with unit prices above THB10 million represents around 20% of total portfolio. Looking forward, the management considers to launch more products in the mid- to high-end pricing segments with housing brands "Preukpirom" and "Laddarom".

We expect this new move from QH coupled with its well-established brands and diversified product portfolio should give the company the flexibility to adjust its products to match market demand in a timely manner and regain market share. However, further deterioration in market position could lead to a downward revision on its ratings. As of March 2022, QH had 71 projects, comprising 57 landed property projects and 14 condominium projects. The value of unsold units (including built and unbuilt units) was worth THB39.5 billion. Landed property projects accounted for 69% of the total remaining value, while the rest comprised ready-to-transfer condominium projects.

Prudent financial management

We expect QH's debt to capitalization ratio to maintain below 35% over the next three years. QH's financial leverage has constantly declined since the company reduced the value of new project launches and land purchases over the past few years amid concerns over the COVID-19 pandemic. As a result, its debt to capitalization ratio at the end of March 2022 further declined to 31%, from around 33% in 2021 and 41%-50% in 2016-2019. In our base-case forecast, we assume QH to launch new landed property projects worth around THB10 billion annually in 2022-2024. The budget for land is set at THB3 billion per year. Apart from the residential property business, we forecast the company to have additional investment in 2024 for lease extension in its rental business. As a result, we expect the debt to capitalization ratio to stay in the 30%-32% range and the debt to EBITDA ratio to hover around 4.5 times over the forecast period. 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. As of March 2022, the ratio was 0.4 times. We believe that QH will easily comply with the financial covenant over the next 12 months.

At the end of March 2022, QH had debts of THB14.7 billion, comprising THB12 billion debentures and THB2.7 billion long-term loans. Around THB2.7 billion of its total debts were considered priority debts. As a result, QH's priority debt to total debt ratio was 19%, less than our 50% threshold. Thus, we view QH's unsecured creditors as not being significantly disadvantaged to its priority debt holders with respect to the priority of claims against the company's assets.

Substantial dividend contribution from investments in affiliates

We consider QH's sizeable portfolio of marketable securities as enhancing its liquidity position. 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%), Quality Houses Leasehold Property Fund (QHLPF, 25.7%), and Quality Houses Hotel and Residence Freehold and Leasehold Property Fund (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 THB1.2-THB1.5 billion per annum. We expect QH to receive dividends from its investments ranging from THB1.1-THB1.3 billion per annum during 2022-2024.

In addition, the market value of these investments is sizable. At the end of March 2022, the portfolio carried a fair value of THB48.1 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 considerably.

Adequate liquidity

We assess QH to have adequate liquidity over the next 12 months. As of March 2022, the company has debts of THB9.1 billion coming due in the next 12 months, comprising THB7.5 billion maturing debentures and THB1.6 billion term loan repayments. The company already repaid THB3.5 billion of debentures due in May 2022 with new debenture issues and internal cash. QH plans to refinance the remaining debentures due in November 2022 with the new issuance of debentures and long-term loans.

QH's sources of liquidity included cash on hand of THB3.9 billion and available short-term credit facilities of around THB4.2 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 THB5.4 billion, which can be pledged as collateral for new credit facilities. In addition, the company already has back-up credit facilities of THB1.5 billion from a financial institution to fund the scheduled bullet repayments in 2022. Going forward, QH intends to control its debentures repayment of THB4-THB5 billion per year.

BASE-CASE ASSUMPTIONS

These are the key assumptions in TRIS Rating's base case forecast for QH's operations during 2022-2024:

- Launch new landed property projects worth around THB10 billion annually.
- Annual budget for land acquisition to be THB3 billion.
- Total operating revenue in the range of THB9-THB10 billion per annum, with an EBITDA margin of around 29%-31%.

RATING OUTLOOK

The "negative" outlook reflects a slower-than-expected recovery in QH's revenue and earnings and its weakened market position in the landed property segment. Amid economic headwinds, QH's operating performance could further decline from its current level.

RATING SENSITIVITIES

We could revise QH's outlook to "stable" if its operating performance improves such that its revenue and EBITDA stay above THB10 billion and THB3 billion on a sustained basis, respectively. At the same time, its financial profile should not further deteriorate from the current level. In contrast, the rating downward revision could occur if QH's operating performance and/or financial profile significantly deteriorate from our base-case expectation causing the debt to capitalization ratio to reach above 50% and the debt to EBITDA ratio to exceed 5 times on a sustainable basis.

COMPANY OVERVIEW

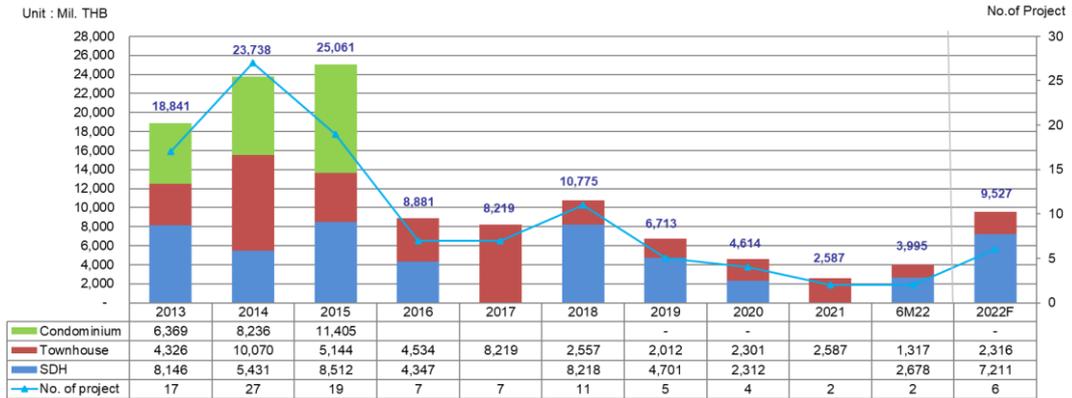
QH was established in 1983 by Land & Houses PLC (LH), the Gaysorn Group, and Dhana Siam Finance and Securities PLC. The company was listed on the Stock Exchange of Thailand (SET) in 1991. As of April 2022, LH was the largest shareholder of QH, holding a 25% stake.

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, THs, 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 THB25 million per unit under the brand "Pruekpirom", the middle- to high-end SDHs with unit prices of THB15-THB25 million under the brand "Laddarom", middle SDHs and semi-DHs with unit prices between THB6-THB15 million under the brand "Vararom" and "Casa Ville", and affordably priced semi-DHs and THs with selling prices between THB2.5-THB6 million per unit under the brand "Q District".

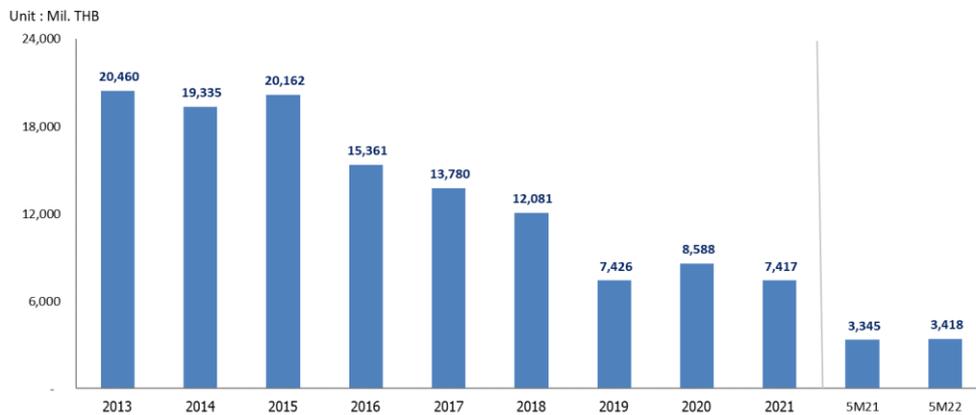
KEY OPERATING PERFORMANCE

Chart 1: New Project Launches



Source: QH

Chart 2: Presales



Source: QH

Chart 3: Revenue Breakdown



Source: QH

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS*

Unit: Mil. THB

	Jan-Mar 2022	-----Year Ended 31 December -----			
		2021	2020	2019	2018
Total operating revenues	2,091	8,120	9,138	10,680	15,888
Earnings before interest and taxes (EBIT)	781	2,460	3,086	3,871	5,199
Earnings before interest, taxes, depreciation, and amortization (EBITDA)	498	2,661	3,108	3,787	4,988
Funds from operations (FFO)	351	2,010	2,237	2,822	3,654
Adjusted interest expense	71	417	533	634	669
Real estate development investments	26,860	27,461	29,706	33,642	35,450
Total assets	46,651	46,236	47,667	50,902	54,164
Adjusted debt	12,106	13,246	15,757	18,949	19,727
Adjusted equity	27,558	26,985	26,568	26,863	26,286
Adjusted Ratios					
EBITDA margin (%)	23.82	32.77	34.01	35.46	31.40
Pretax return on permanent capital (%)	5.89 **	5.57	6.65	7.90	10.54
EBITDA interest coverage (times)	7.02	6.38	5.83	5.97	7.45
Debt to EBITDA (times)	4.35 **	4.98	5.07	5.00	3.95
FFO to debt (%)	17.46 **	15.17	14.20	14.89	18.52
Debt to capitalization (%)	30.52	32.93	37.23	41.36	42.87

* Consolidated financial statements

** Annualized with trailing 12 months

RELATED CRITERIA

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

Quality Houses PLC (QH)

Company Rating:	A-
Issue Ratings:	
QH22NA: THB4,000 million senior unsecured debentures due 2022	A-
QH243A: THB3,000 million senior unsecured debentures due 2024	A-
QH246A: THB1,500 million senior unsecured debentures due 2024	A-
QH255A: THB1,000 million senior unsecured debentures due 2025	A-
Rating Outlook:	Negative

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