

# QUALITY HOUSES PLC

No. 120/2021

30 July 2021

## CORPORATES

<b>Company Rating:</b>	A-
<b>Issue Ratings:</b>	
Senior unsecured	A-
<b>Outlook:</b>	Stable

**Last Review Date:** 11/05/21

### 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-", with a "stable" rating outlook. The ratings reflect QH's diverse product portfolio, moderately strong competitive position in the landed property segment, stable dividend income from its investments in affiliates, and relatively low financial leverage. The ratings also take into consideration our concerns over the prolonged Coronavirus Disease (COVID-19) pandemic, which continues to pressure the company's operating performance in both residential property development and hospitality businesses.

## KEY RATING CONSIDERATIONS

### Prolonged COVID-19 pandemic pressures 2021 performance

We expect QH's operating performance to remain under pressure in 2021, due to the intense competition in the residential market and the poor performance of its hotel operations during the pandemic. In our view, the ongoing COVID-19 pandemic and slow vaccination rate will dampen recovery of the residential property market and hospitality business throughout 2021. The lockdown measures and 30-day closure of construction sites in Bangkok in response to the latest escalation of outbreaks could lead to delays in new project launches and housing transfers to homebuyers.

Amid the uncertainty, QH's strategy is to focus on clearing its inventory and reduce new project launches. Project launches in 2020 dropped by 31% year-on-year (y-o-y) to THB4.61 billion. Due to the resurgence of COVID-19 outbreaks, the company plans to launch only three new landed residential projects worth THB5.33 billion in 2021. However, the company aims to launch new landed property projects worth around THB10 billion per annum during 2022-2023 in order to sustain revenue growth.

As QH focuses mainly on the development of landed property projects, its backlog was minimal. Thus, revenue from residential sales depends largely on the company's ability to generate new sales and transfers each year. As a result, we expect QH's total operating revenue to stay around THB9 billion in 2021 and recover to range between THB10-THB11 billion per annum during 2022-2023. The revenue contribution from the residential property business is expected to be 91%-93% of the company's total operating revenue over the next three years.

### Expected softening earnings

We expect its profitability to soften in the short- to medium-term due to lower margins in residential projects and depressed results from the hospitality business. We forecast lower gross profit margins in the residential property business from promotional campaigns and price reduction for its slow-moving projects, especially condominium projects. In addition, we expect its hospitality business to incur operating losses this year and take time to recover to pre-COVID-19 levels. Although its two hotels, Centre Point Hotel Silom and Centre Point Hotel Pratunam, have joined Alternative State Quarantine (ASQ), the revenue may not be sufficient to cover fixed costs. However, its lower selling, general, and administrative (SG&A) expenses and profit sharing from affiliates should partly offset the impact of the margin drop.

Under our base-case forecast, we expect QH's total gross profit margin to stay in the 29.5%-31% range during 2021-2023. We view the company's share of profits from its investments to constitute the majority contribution to QH's earnings. We forecast profit sharing from affiliates to range between THB1.48-THB1.71 billion per annum over the next three years. Its earnings before interest, taxes, depreciation, and amortization (EBITDA) is expected to range between THB2.67-THB3.21 billion per annum, with an EBITDA margin of 28%-30% over the forecast period.

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

QH's product portfolio is well-diversified in terms of product type variety and price ranges. The company offers single-detached houses (SDH), townhouses, and condominiums to homebuyers across market segments. Its products cover the middle- to high-end pricing segments with selling prices ranging from THB3 million to THB60 million. In our view, its market position in the landed property segment is comparatively stronger than the condominium segment. QH's housing brands, such as "Laddarom", "Preukpirom", "Vararom", and "Casa", are broadly accepted among homebuyers. QH's market share ranked 11<sup>th</sup> among SET-listed property developers based on operating revenue.

We view the competition among residential property developers become increasingly intense. Therefore, QH needs to quickly adjust its products and marketing strategy in order to maintain its competitive position in the market. With its well-established brands and diversified product portfolio, the company should be able to adjust its products to match market demand. However, a further decline in its market share could negatively impact its rating or outlook in the medium term. As of March 2021, QH had 77 projects, comprising 63 housing projects and 14 condominium projects. The value of unsold units was worth THB40.96 billion. Landed property projects accounted for 69% of the total remaining value, while the rest was ready-to-transfer condominium projects.

#### **Prudent financial policy**

We expect QH to maintain its financial leverage at the current level over the next three years. The company's financial burden has declined during the downturn. At the end of March 2021, its debt to capitalization ratio was 36%, dropped from around 41%-50% in 2016-2019. As the company plans to launch only landed property projects which require less capital than high-rise condominium projects, we forecast its debt to capitalization ratio to stay below 50% during 2021-2023. In our base-case forecast, we assume QH to launch new landed property projects worth THB5.33 billion in 2021 and THB10 billion per annum in 2022-2023. The budget for land is expected to be around THB3 billion per annum over the next three years. Apart from the residential property business, we project the company to have additional investment in 2022 for lease extension in its rental business. As a result, we expect the debt to capitalization ratio to be in the 35%-37% range and the debt to EBITDA ratio to be 5-6 times during 2021-2023.

As of June 2021, QH had THB16.04 billion in debt, including THB3.74 billion of priority debt. QH's priority debt to total debt ratio was then 23%. As the ratio of priority debt to total debt was lower than the 50% threshold, we view QH's unsecured creditors are not significantly disadvantaged with respect to the priority of claim against its assets.

The financial covenant on QH's debt obligations requires QH to maintain its net interest-bearing debt to equity ratio below 2 times. The ratio at the end of March 2021 was 0.5 times. We believe the company should have no problems complying with this financial covenant over the next 12 months.

#### **Sizable dividend income from investments in affiliates**

We view QH's sizeable portfolio of marketable securities as an enhancement of 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 provide dividends to QH on a recurring basis. Over the past five years, QH recognized share of profits from its investments of THB1.53-THB1.93 billion per annum and received dividends of THB1.06-THB1.45 billion per annum. We expect QH to receive dividends from its investments ranging from THB1-THB1.3 billion per annum over the next three years.

In addition, the market value of these investments is significant. At the end of March 2021, the portfolio carried a fair value of THB44.7 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.

#### **Adequate liquidity**

We assess QH to have adequate liquidity for the next 12 months. At the end of May 2021, QH has debts coming due over the next 12 months of THB6 billion, comprising THB4.5 billion in debentures, THB500 million in bills of exchange (B/Es), and THB1 billion in long-term loans. The company already repaid THB1 billion of debentures due in June 2021 with new debentures. QH plans to refinance the remaining debentures due in May 2022 with new issuance of debentures and/or

long-term loans. The outstanding B/Es will be repaid with internal cash.

QH's sources of liquidity at the end of May 2021 comprised cash on hand of around THB1.95 billion and available short-term credit facilities of around THB4.21 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 cost worth THB2.8 billion, which can be pledged as collateral for new credit facilities. Going forward, QH intends to manage its debentures repayment below THB5-THB6 billion per year and seek long-term credit facilities from financial institutions as back-up funding source. The company already has back-up credit facilities of around THB2 billion from a financial institution to fund the scheduled bullet repayments in 2022. QH is also in the process of seeking further long-term credit facilities with other financial institutions.

#### BASE-CASE ASSUMPTIONS

These are the key assumptions in TRIS Rating's base case forecast:

- Operating revenue in the range of THB9-THB11 billion per annum during 2021-2023.
- Gross profit margin to range between 29.5%-31% and the EBITDA margin in the range of 28%-30% over the next three years.
- Land acquisition budget of THB3 billion per year during 2021-2023.

#### RATING OUTLOOK

The "stable" outlook on QH reflects our expectation that the company will maintain its operating performance as targeted and keep its financial position at the current level. TRIS Rating expects QH to generate revenues of THB9-THB11 billion per annum during 2021-2023. The company should maintain the debt to capitalization ratio below 50% and the debt to EBITDA below 6 times in 2021-2023. The EBITDA margin is expected to be in the 28%-30% range over the next three years.

#### RATING SENSITIVITIES

The ratings and/or outlook of QH could come under downward pressure if its operating performance and/or financial profile deteriorate significantly from our base-case forecasts, such that the debt to capitalization ratio stays above 60%, and the debt to EBITDA ratio higher than 6 times for an extended period. In contrast, the ratings and/or outlook could be revised upward if the company could improve its operating performance significantly, while its financial profile does not deteriorate from current levels.

#### COMPANY OVERVIEW

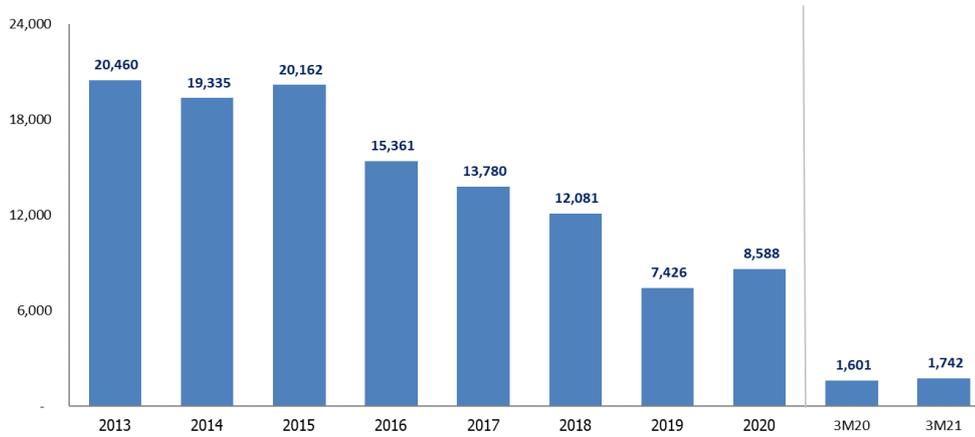
QH was established in 1983 by Land & Houses PLC (LH), the Gaysorn Group, and Dhana Siam Finance and Securities PLC. The company was listed on the Stock Exchange of Thailand (SET) in 1991. As of April 2021, LH was the largest shareholder of QH, holding a 25% stake.

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 single-detached house (SDH), semi-detached houses (Semi-DH), 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 single-detached houses, 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 townhouses priced at THB2-THB4 million per unit. In 2020, QH is introducing the "Q Prime" brand for townhouses in the premium segment priced at THB6-THB7 million per unit.

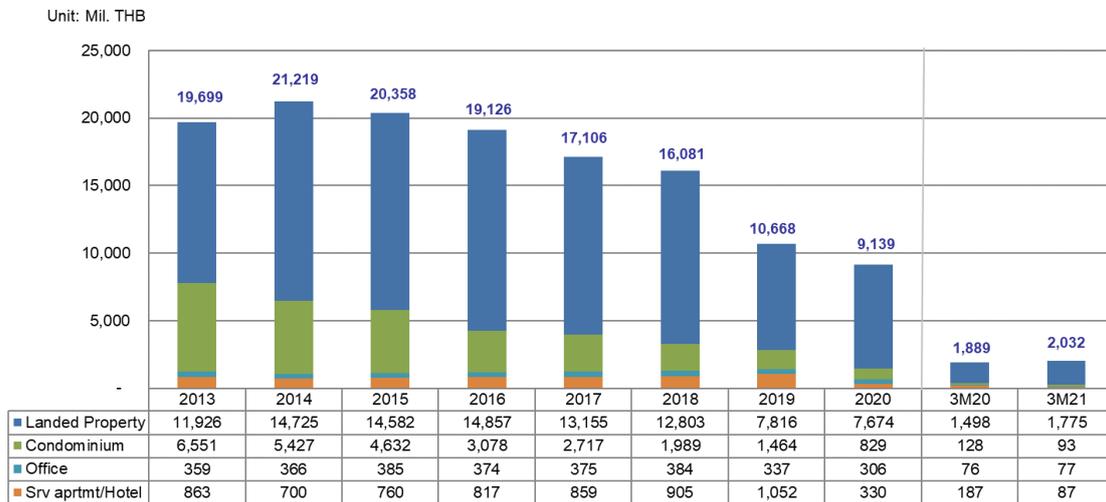
**KEY OPERATING PERFORMANCE**

**Chart 1: Presales Performance**



Source: QH

**Chart 2: Revenue Breakdown**



Source: QH

**FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS\***

Unit: Mil. THB

	Jan-Mar 2021	-----Year Ended 31 December -----			
		2020	2019	2018	2017
Total operating revenues	2,032	9,138	10,680	15,888	17,106
Earnings before interest and taxes (EBIT)	633	3,086	3,871	5,199	4,038
Earnings before interest, taxes, depreciation, and amortization (EBITDA)	374	3,108	3,787	4,988	3,962
Funds from operations (FFO)	242	2,291	2,858	3,779	2,772
Adjusted interest expense	84	533	634	669	847
Real estate development investments	28,923	29,706	33,642	35,450	35,895
Total assets	47,696	47,667	50,902	54,164	53,059
Adjusted debt	14,964	15,768	18,949	19,727	19,986
Adjusted equity	26,905	26,568	26,863	26,286	24,802
<b>Adjusted Ratios</b>					
EBITDA margin (%)	18.41	34.01	35.46	31.40	23.16
Pretax return on permanent capital (%)	6.31 **	6.65	7.90	10.54	8.26
EBITDA interest coverage (times)	4.45	5.83	5.97	7.45	4.68
Debt to EBITDA (times)	4.93 **	5.07	5.00	3.95	5.04
FFO to debt (%)	14.92 **	14.53	15.08	19.16	13.87
Debt to capitalization (%)	35.74	37.24	41.36	42.87	44.62

\* Consolidated financial statements

\*\* Annualized with trailing 12 months

**RELATED CRITERIA**

- Issue Rating Criteria, 15 June 2021
- Rating Methodology – Corporate, 26 July 2019
- Key Financial Ratios and Adjustments, 5 September 2018

**Quality Houses PLC (QH)**

<b>Company Rating:</b>	A-
<b>Issue Ratings:</b>	
QH225A: THB3,500 million senior unsecured debentures due 2022	A-
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-
<b>Rating Outlook:</b>	Stable

**TRIS Rating Co., Ltd.**

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