

VILLA KUNALAI PLC

No. 11/2024
15 February 2024

CORPORATES

Company Rating: BB-
Outlook: Stable

Last Review Date: 22/02/23

Company Rating History:		
Date	Rating	Outlook/Alert
24/02/22	BB	Stable

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RATIONALE

TRIS Rating downgrades the company rating on Villa Kunalai PLC (KUN) to “BB-” from “BB”, with a “stable” rating outlook. The rating downgrade reflects a material deterioration in KUN’s operating and financial performances, coupled with our concerns over the volatility of its revenue and earnings. The rating also incorporates the negative impacts of interest rate hikes, high household debt, and the reimposition of stringent loan-to-value (LTV) rules in 2023 which could suppress housing demand in the short to medium term.

The rating continues to reflect KUN's small business scale; portfolio concentration in terms of number of projects, location, and segmentation; relatively high financial leverage; as well as tight liquidity.

KEY RATING CONSIDERATIONS

Weaker-than-expected operating results

KUN’s operating performance in the first nine months of 2023 (9M23) fell significantly below our expectation. The company reported total operating revenue of THB557 million in 9M23, achieving only 48% of our prior full-year forecast. Revenue from single-detached house (SDH) and semi-detached house (Semi-DH) products reached around half of our prior full-year target, while revenue from townhouse (TH) and commercial building (CB) units reached 35%, reflecting unfavorable market sentiment in the residential property market and high rejection rates from banks.

In addition, KUN’s profitability has been pressured by intense competition among the leading property developers. The company sacrificed profit margins in some projects in an attempt to boost sales. As a result, KUN posted earnings before interest, taxes, depreciation, and amortization (EBITDA) of only THB80 million in 9M23, significantly deviating from our prior full-year forecast of THB230 million. EBITDA margin weakened to 14% in 9M23 from 18%-23% in 2020-2022 while funds from operations (FFO) turned negative, significantly lower than our prior forecast of around THB100 million per annum. Its bottom line fell to 7% of total operating revenue in 9M23, from 11%-16% in 2020-2022.

Future revenue and earnings hinge on a few projects

KUN’s limited operational scale with only a few active projects concentrated in specific locations poses a significant constraint on its credit profile. Negative market responses in one or two projects could have a significant impact on the company's overall performance.

KUN’s residential project portfolio as of December 2023 comprised 10 on-going projects situated in three locations; the Rangsit, Bang Khun Thian, and Bang Bua Thong areas. Total unsold project value (including built and unbuilt units) amounted to THB11.6 billion. Of the unsold value, 57% was from a single project in the Rangsit area, 29% from a project in the Bang Khun Thian area, and the remainder from projects in the Bang Bua Thong area.

Our base-case scenario projects a drop in KUN’s total operating revenue in 2023 of 25% year-on-year (y-o-y). Its revenue is expected to improve to the THB0.9-THB1.0 billion level in 2024-2025. Around 75% of the projected revenue in 2023 will come from the projects in the Bang Bua Thong area. However, around 60%-70% of estimated revenue in 2024-2025 hinges on the performances of two large projects in the Rangsit and Bang Khun Thian areas. These projects were launched in 2022-2023 and do not yet have a proven track

record. In addition, these locations are already characterized by intense competition among the top-tier property developers. As a result, KUN's revenue in 2024-2025 could be more volatile than expected.

We project KUN's EBITDA to weaken to around THB100 million in 2023 with an EBITDA margin of 13%. Its EBITDA should improve to around THB200 million per annum in 2024-2025 with an EBITDA margin of 18%-20% as we anticipate that the two projects in the Rangsit and Bang Khun Thian areas will generate stronger profits than those in the Bang Bua Thong area. Our projected higher profit margin should be driven by the relatively low land costs of these two projects and stable construction material prices.

Relatively high financial leverage

We expect KUN's financial leverage at the end of 2023 to stand at a relatively high level and its cash flow protection to remain in negative territory following its ongoing aggressive expansion. In 2021-2023, KUN purchased two large land plots in the Bang Khun Thian and the Rangsit areas with a total purchasing price of around THB1 billion. The company launched two new projects on these land plots with combined project value of THB10.2 billion. With its comparatively small capital base and weaker operating performance, KUN's debt to capitalization ratio surged to 68% as of September 2023, from 62% in 2022 and 56% in 2021. Its FFO to debt ratio fell into negative territory in 9M23, from 8% in 2022 and 19% in 2021.

Looking forward, KUN's leverage is expected to improve gradually. Its debt to capitalization ratio should improve to 60%-63% and its FFO to debt ratio should revive to 2%-3% in 2024-2025. This is based on our assumption that KUN will launch only one project worth THB0.4 billion in 2024. We also assume that there will be no new land plot acquisitions in 2024-2025 since KUN will take several years to develop these two large projects. We estimate its annual capital expenditures for construction of around THB500 million per annum in the next two years.

At the end of September 2023, KUN's total debt stood at THB1.8 billion. Priority debt, including secured debt at the company and its subsidiaries, was THB933 million. This translates to a priority debt to total debt ratio of 52%. Thus, in our view, KUN's unsecured creditors are significantly disadvantaged to its priority debt holders with respect to the priority of claims against the company's assets.

Interest rate hikes directly impact KUN's targeted customers

The Bank of Thailand (BOT) raised the policy rate by 100 basis points (bps) to 2.5% in 2023. We view that rising interest rates will affect not only the funding costs of developers but also the debt servicing capacity of homebuyers, especially those in the middle- to low-income segments. Bank rejection rates among low-income homebuyers tend to increase amid concerns over high household debt. Rising interest rates could also dampen demand from investors as their expected returns would be eroded by higher funding costs. However, we do not expect the proportion of demand from investors and/or speculative demand to increase.

The reimposition of stringent LTV rules in 2023 could also soften housing demand in the short to medium term. In our view, the LTV rules will generally have a greater impact on the middle- and high-end segments since these buyers may have more than one mortgage contract. However, the impact of the LTV measures on KUN is likely to be relatively low as its key customers are first-time homebuyers in the middle- and low-income segments.

Tight but manageable liquidity

We assess KUN's liquidity to be tight but manageable over the next 15 months. Debt maturing in the fourth quarter of 2023 through 2024 will amount to THB958 million, comprising THB680 million long-term project loans, THB200 million debentures, THB50 million short-term promissory notes (P/N), and THB28 million long-term loans. KUN's sources of liquidity at the end of September 2023 included cash on hand of THB97 million and undrawn unconditional committed credit facilities of THB197 million. In addition, KUN had unencumbered land banks at book value of THB88 million and inventory of THB282 million, which could be pledged as collaterals for new loans (if needed).

Project loans are normally repaid with the proceeds from the underlying projects' unit transfers. KUN usually refinances its matured debentures by new debenture issuances and rolls over its matured short-term borrowings. To avoid its exposure to refinancing risk, KUN intends to sell some land plots within this year. If successful, this would alleviate pressure on the company's financial profile.

The financial covenants on KUN's debentures require the company's net interest-bearing debt to equity (net IBD/E) ratio to remain below 3 times. The ratio at the end of September 2023 was 2.1 times. We believe that the company should have no problems remaining in compliance with the financial covenants over the next 12 to 18 months.

BASE-CASE ASSUMPTIONS

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

- KUN launched new landed property projects worth THB7.2 billion in 2023 and expect to launch new project worth THB0.4 billion in 2024.
- No new land plot acquisitions in 2024-2025, after having land acquisition budget of THB450 million in 2023.
- Total operating revenue to decline by 25% y-o-y in 2023 before reviving to the THB0.9-THB1.0 billion level in 2024-2025.
- EBITDA margin to shrink to 13% for the full year of 2023, but improving to 18%-20% in 2024-2025.

RATING OUTLOOK

The "stable" outlook reflects our expectation that KUN will be able to deliver operating performance and maintain its financial profile as targeted. We expect KUN's EBITDA to weaken to around THB100 million for the full year 2023, but this should improve to around THB200 million per annum from 2024 onwards, with an EBITDA margin of 18%-20%. We also expect KUN's debt to capitalization ratio to hang at 60%-68% in 2023-2025 and FFO to debt ratio to stay in negative territory in 2023, but it should increase to 2%-3% in 2024-2025.

RATING SENSITIVITIES

The rating and/or outlook could be revised downward should KUN's operating results and/or financial profile turn out to be worse than our expectations. A negative change to the rating might also be considered if there is any heightened liquidity concern and/or elevated refinancing risk.

On the other hand, a credit upside scenario could emerge if KUN is able to deliver significantly stronger operating results than the target levels and improve its financial profile such that the debt to capitalization ratio stays below 60% and FFO to debt ratio hovers around 10% on a sustained basis.

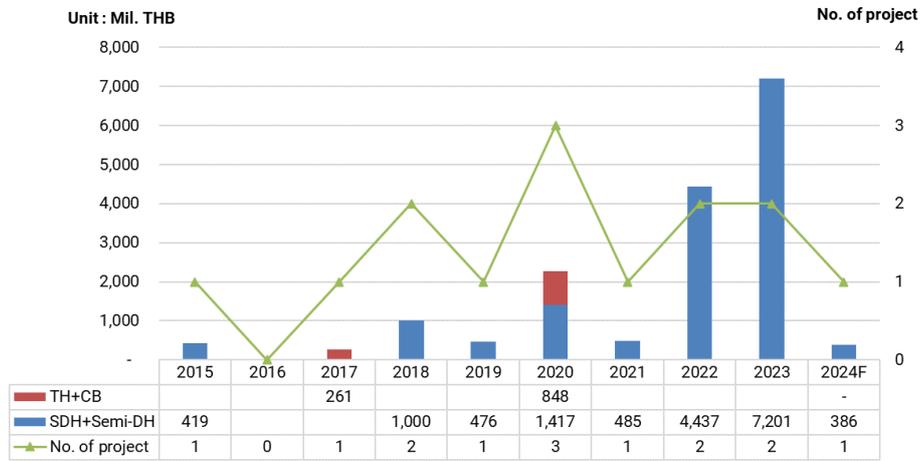
COMPANY OVERVIEW

KUN was established in 2007 by Mrs. Praweerat Dheva-aksorn and Mr. Kuna Dheva-aksorn to operate the property development for sale business. The company became a public company in February 2019 and was listed on the Stock Exchange of Thailand (SET) in December 2019. The Dheva-aksorn Family and Sangkawanich Family, the company's founders and major shareholders, held a combined 73% equity stake as of September 2023. KUN focuses on the middle- to low-income housing segments. The company offers SDH and semi-DH units with average selling price of THB3-THB6 million per unit, TH with unit price of around THB2 million, and CB with unit price of THB3-THB4 million. Before 2022, KUN's housing projects were in the Bang Bua Thong area and Chacherngsao province. Since then, the company has explored other areas in order to diversify its project locations and product segments. The company expanded its property portfolio in the Bang Khun Thian area in 2022 and the Rangsit area in 2023 as well as tapped the higher-income segment with unit prices of THB6-THB10 million.

As of December 2023, KUN's residential project portfolio comprised ten on-going projects, with a remaining value of THB11.6 billion and a backlog value of THB108 million. Around 57% of the remaining value is located in the Rangsit area, 29% in the Bang Khun Thian area, and the remainder in the Bang Bua Thong area.

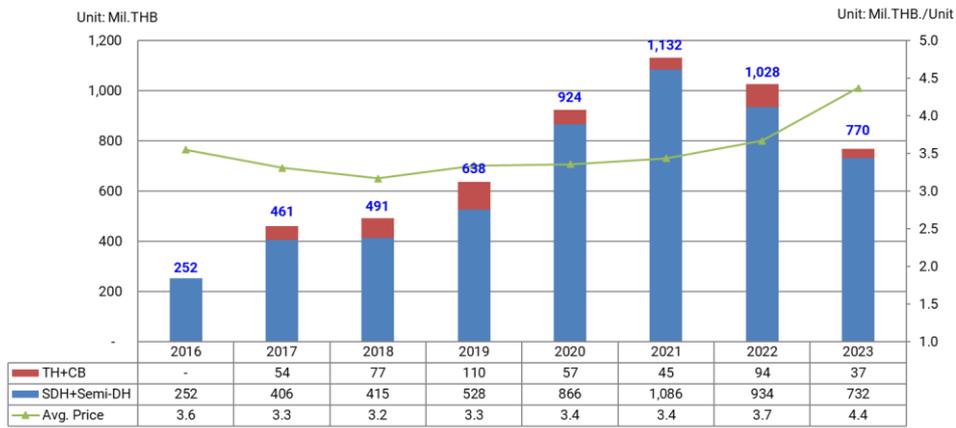
KEY OPERATING PERFORMANCE

Chart 1: New Project Launches



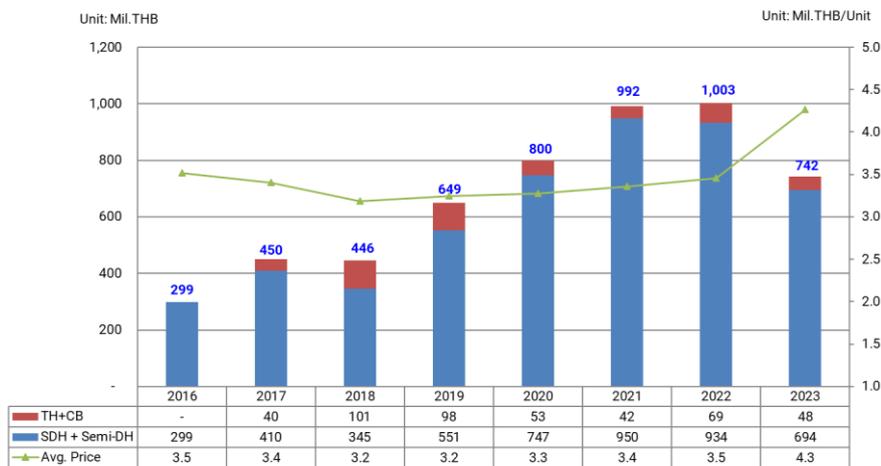
Source: KUN

Chart 2: Presales



Source: KUN

Chart 3: Transfers



Source: KUN

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS*

Unit: Mil. THB

	Jan-Sep 2023	-----Year Ended 31 December -----			
		2022	2021	2020	2019
Total operating revenues	557	1,005	996	804	653
Earnings before interest and taxes (EBIT)	75	175	223	141	94
Earnings before interest, taxes, depreciation, and amortization (EBITDA)	80	182	230	148	102
Funds from operations (FFO)	(13)	85	151	99	58
Adjusted interest expense	83	70	39	27	31
Real estate development investments	2,494	1,678	1,481	797	781
Total assets	2,815	2,267	1,822	1,035	940
Adjusted debt	1,696	1,050	780	246	291
Adjusted equity	790	641	623	513	459
Adjusted Ratios					
EBITDA margin (%)	14.3	18.1	23.1	18.4	15.7
Pretax return on permanent capital (%)	5.0 **	9.9	18.3	16.7	12.7
EBITDA interest coverage (times)	1.0	2.6	5.9	5.5	3.3
Debt to EBITDA (times)	14.9 **	5.8	3.4	1.7	2.8
FFO to debt (%)	(0.3) **	8.1	19.4	40.2	19.9
Debt to capitalization (%)	68.2	62.1	55.6	32.4	38.8

* 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

Villa Kunalai PLC (KUN)

Company Rating:

BB-

Rating Outlook:

Stable

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