

HOME PRODUCT CENTER PLC

No. 200/2019
6 December 2019

CORPORATES

Company Rating: AA-
Outlook: Stable

Last Review Date: 06/12/18

Company Rating History:

Date	Rating	Outlook/Alert
06/12/18	AA-	Stable
29/11/17	A+	Positive
18/11/11	A+	Stable
17/11/10	A	Positive
22/10/08	A	Stable
23/01/07	A-	Stable
15/10/04	BBB+	Stable
12/07/04	BBB	Positive
05/11/03	BBB	-

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RATIONALE

TRIS Rating affirms the company rating on Home Product Center PLC (HMPRO) at “AA-” with a “stable” outlook. The rating reflects HMPRO’s strong market position in the home improvement retail business in Thailand, together with its improvements in margins and sizable cash flow. The rating also takes into consideration the challenges posed by intensifying competitive pressures and decelerating economic growth in Thailand.

KEY RATING CONSIDERATIONS

Strong market position with continued sales growth and sustainable margin

HMPRO is the leading home improvement retailer in Thailand, ranked first in the industry in terms of total sales for more than a decade. The top six operators in the industry are “HomePro”, CRC Group (“Homework” and “Thai Wasadu”), “Siam GLOBAL House”, “Do Home”, “Boon Thavorn”, and “Index Living Mall”.

HMPRO’s total sales rose to Bt61.6 billion in 2018 from Bt18.5 billion in 2008, a compound annual growth rate of 13.5%. HMPRO’s profitability has ranked above the industry average. The earnings before interest, tax, depreciation, and amortization (EBITDA) margin has been in the 14.0%-16.5% range for the last five years, higher than the 8%-9% average of other major players.

Same-store sales remain subdued

The current low rate of growth in the Thai economy combined with prolonged weak farm prices have negatively affected the same-store sales growth of most home improvement retailers, including HMPRO. HMPRO’s same-store sales grew by 1.1% year-on-year (y-o-y) in 2018 and rose by 2.2% y-o-y in the first nine months of 2019. The rise in 2019 was attributed to higher sales of cooling and anti-air pollution products. However, TRIS Rating expects the ongoing and persistent economic slowdown to dampen domestic demand in 2019. The Bank of Thailand (BOT) forecasts the country’s gross domestic product (GDP) will grow by 2.8% in 2019, a decline from 4.1% in 2018. Private consumption in Thailand is projected to grow by 3.8% in 2019, down from 4.6% in 2018.

TRIS Rating forecasts HMPRO’s total sales to rise by 1.4% y-o-y in 2019, and grow by 4% per year during the 2020-2022 periods. The EBITDA margin is projected to hover around 14% over the next few years.

Change in product mix to enhance margins

HMPRO’s gross margin continued to improve to 29.3% during the first nine months of 2019, up from 28.7% over the same period of the prior year. The improved gross margin was driven by a change in HMPRO’s product mix. Sales of house brands and imported brands, which carry higher margins, accounted for 19%-20% of sales in 2018 through the first nine months of 2019. HMPRO aims to increase the proportion of house brands and imported brands to 25% of sales in the longer term.

Manageable selling and administrative expenses

HMPRO has tried to improve control over its selling, general and administrative expenses (SG&A). The ratio of SG&A to sales has remained relatively unchanged in the range of 21%-22% over the last five years. Additional depreciation expenses from a new distribution center in 2019

should be more than offset by better cost efficiency across all formats and cost controls covering logistics and utility management.

Financial leverage rises, but remains acceptable

HMPRO's total debt to capitalization ratio rose to 45.3% at the end of September 2019, up from 43.4% at the end of 2018 as HMPRO spent more on planned capital expenditures.

HMPRO plans to open 111-150 stores across all store formats in the medium term. Annual capital expenditure is forecast to be Bt4-Bt5 billion during 2019-2022, up from Bt2.9 billion in 2018. Hence, the debt to capitalization ratio is forecast to remain in the range of 42%-45% during 2019-2022, from 43.4% in 2018.

The capital expenditures will be funded by cash flow from operations and new borrowings. TRIS Rating expects HMPRO's cash flow protection to remain strong. The ratio of funds from operations (FFO) to total debt is expected to remain in the range of 46%-52% over the next few years.

Adequate liquidity

HMPRO has a negative cash cycle which means it has surplus working capital. The company has high negotiating power over its suppliers, derived from its strength in economies of scale, while inventory levels and accounts receivable are kept under careful control.

TRIS Rating expects HMPRO to maintain adequate liquidity over the next 12 months. Our base-case forecast assumes EBITDA of Bt9.5-Bt10 billion per annum. The company has scheduled debt repayments of Bt4-Bt6 billion per year during 2019-2022. At the end of September 2019, cash on hand and short-term investments stood at Bt2.3 billion.

BASE-CASE ASSUMPTIONS

- Total sales to grow by 1%-4% in 2019-2022.
- Gross profit and EBITDA margins to be 30% and 14%, respectively.
- Total capital spending to be around Bt4-Bt5 billion per year in 2019-2022.
- Other assumptions are in line with historical trends.

RATING OUTLOOK

The "stable" outlook reflects TRIS Rating's expectation that HMPRO will remain Thailand's leading home improvement retailer. We expect the company's leverage to remain at an acceptable level even as the company continues to grow.

RATING SENSITIVITIES

The rating could be upgraded if the company enlarges cash flow generation while maintaining a strong balance sheet. In contrast, HMPRO's rating could be revised downward if financial performance is weaker than expected or if leverage is significantly higher, either as a result of an aggressive expansion or a drop in operating performance.

COMPANY OVERVIEW

Founded in 1995 and listed on the Stock Exchange of Thailand (SET) in 2001, HMPRO is the leading home improvement retailer in Thailand. The company owns and operates one-stop shopping home centers under the trade names "HomePro" and "MegaHome", which are the company's trademarks. As of September 2019, its major shareholders were Land and Houses PLC (LH) (30%) and Quality Houses PLC (QH) (20%).

The company caters primarily to do-it-yourself homeowners by offering home-related products, such as home improvement products, bathroom and sanitary wares, kitchen equipments, home appliances, audio visual equipments, electrical and lighting products, and home décor products.

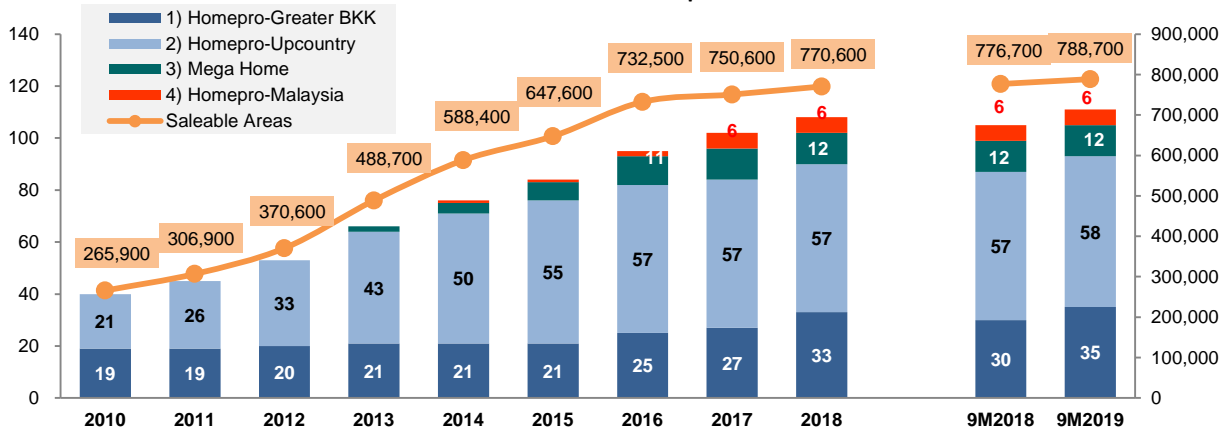
HMPRO owns three types of store; HomePro stores, Mega Home stores, and HomePro S stores. A typical HomePro store, the company's initial retailing format, offers a wide range of home-related products and services with a store area of 3,000-12,000 square meters (sq.m.). A Mega Home store is a large-scale warehouse-style store, designed to serve the needs of contractors, construction project owners, resellers, and end-users, with a store area of 10,000-20,000 sq.m.

Recently, HMPRO introduced a new store format called "HomePro S". A HomePro S store is a small store, located in a shopping mall, with a store area ranging around 1,200-1,500 sq.m. A HomePro S store is designed under the "small, selected, and service" concepts to serve urban customers and condominium residents with variety of home-related products that match a metropolitan lifestyle. A HomePro S store still offers service just like the original format, a HomePro store.

HMPRO has expanded continuously. As of September 2019, the company operated 111 stores under the HomePro and HomePro S formats: 35 in Greater Bangkok, 58 upcountry, and six stores in Malaysia. The company operates 12 MegaHome stores: two in Greater Bangkok and 10 upcountry. The total saleable area covers 788,700 sq.m.

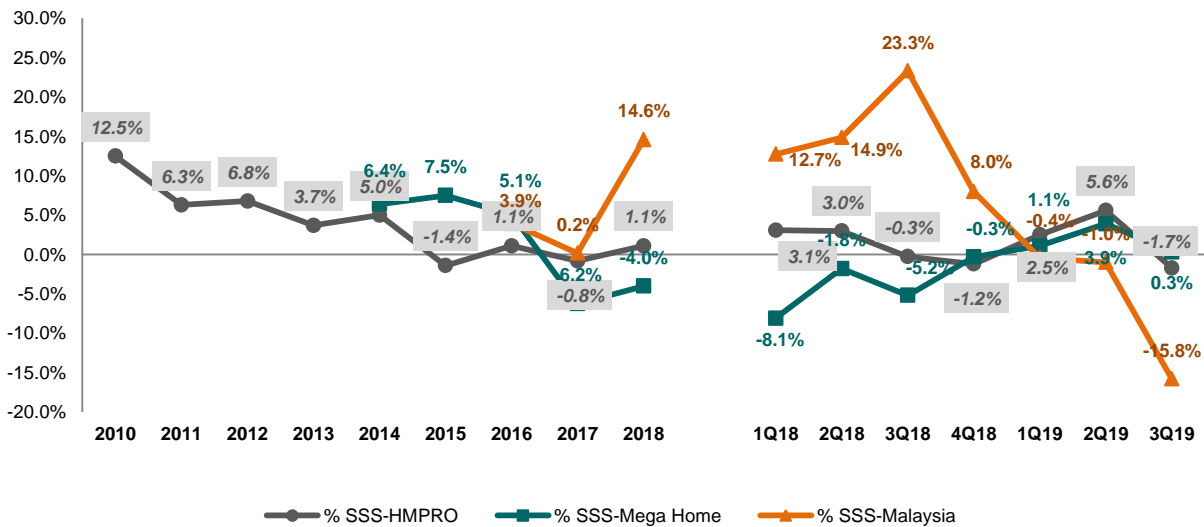
KEY OPERATING PERFORMANCE

Chart 1: HMPRO's Expansion



Source: HMPRO

Chart 2: Same-Store Sales (Y-O-Y)



Source: HMPRO

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS

Unit: Bt million

	Jan-Sep 2019	-----Year Ended 31 December -----			
		2018	2017	2016	2015
Total operating revenues	50,494	66,050	64,234	61,144	56,243
Earnings before interest and taxes (EBIT)	5,972	7,602	6,669	5,776	5,121
Earnings before interest, taxes, depreciation, and amortization (EBITDA)	8,295	10,826	9,739	8,719	7,888
Funds from operations (FFO)	6,751	8,837	7,956	7,069	6,266
Adjusted interest expense	515	680	682	681	704
Capital expenditures	2,438	2,914	3,266	5,143	4,807
Total assets	50,542	54,811	50,949	51,746	46,991
Adjusted debt	16,141	15,281	16,634	16,012	14,091
Adjusted equity	19,476	19,914	18,635	17,490	16,903
Adjusted Ratios					
EBITDA margin (%)	16.43	16.39	15.16	14.26	14.02
Pretax return on permanent capital (%)	22.75	19.20	17.78	16.29	15.62
EBITDA interest coverage (times)	16.10	15.92	14.28	12.81	11.20
Debt to EBITDA (times)	1.42	1.41	1.71	1.84	1.79
FFO to debt (%)	57.21	57.83	47.83	44.15	44.46
Debt to capitalization (%)	45.32	43.42	47.16	47.79	45.46

RELATED CRITERIA

- Rating Methodology – Corporate, 26 July 2019
- Key Financial Ratios and Adjustments, 5 September 2018
- Group Rating Methodology, 10 July 2015

Home Product Center PLC (HMPRO)

Company Rating:	AA-
Rating Outlook:	Stable

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