

M.K. REAL ESTATE DEVELOPMENT PLC

No. 64/2022
26 April 2022

CORPORATES

Company Rating: BBB-
Outlook: Negative

Last Review Date: 21/04/21

Company Rating History:

Date	Rating	Outlook/Alert
10/04/20	BBB-	Stable
12/04/19	BBB	Negative
10/02/16	BBB	Stable
24/06/15	BBB+	Alert Negative
17/06/15	BBB+	Negative
05/03/10	BBB+	Stable
20/03/08	BBB	Stable

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RATIONALE

TRIS Rating affirms the company rating on M.K. Real Estate Development PLC (MK) at “BBB-”. At the same time, TRIS Rating revises the company’s rating outlook to “negative” from “stable”. The “negative” outlook reflects MK’s weaker-than-expected operating performance and the anticipated slow recovery of its residential property and wellness businesses amid the prolonged Coronavirus Disease 2019 (COVID-19) pandemic. The rating continues to reflect MK’s relatively small revenue base, rising contribution from the industrial estate business (IE business), and high financial leverage.

KEY RATING CONSIDERATIONS

Weaker-than-expected operating performance

MK’s operating revenues in 2021 reached only THB3 billion, significantly lower than our previous forecast of THB4.2 billion. Its gross profit margin was only 20%, a further drop from 32% in 2019 and 29% in 2020, due to very thin profit margin on land sales and a loss incurred by the wellness business. As a result, the company’s funds from operations (FFO) deteriorated to minus THB247 million, from THB432 million in 2019 and THB229 million in 2020.

MK’s weak performance was mainly due to a sharp drop in residential sales amid intense competition and a lack of new project launches over the past two years. Housing sales hit a low of THB1.6 billion, down by 36% year-on-year (y-o-y) from THB2.5 billion in 2020. In addition, the company’s wellness business was negatively affected by the lingering COVID-19 pandemic, which led to lower numbers of foreign tourists than expected. However, the operating performance of MK’s IE business was in line with targets.

Small revenue base with slow recovery in residential property and wellness businesses

Looking forward, we do not expect a significant change in MK’s revenue base from the current level. Revenues in 2021 reached only THB3 billion, deriving from residential property 53%, land sales 30%, and IE and wellness businesses 17%. Under our base-case forecast, we project MK’s total operating revenue to range between THB2.2-THB3.2 billion per annum during 2022-2024. The revenue contribution from residential property and land sales is expected to be 65%-75% of the total while revenue from the IE and wellness businesses should increase to 25%-35%.

We expect MK’s residential property sales to remain stagnate over the next 2-3 years. The company has no concrete plans for new project launches. Thus, revenues from the residential property business will mainly come from the sale of remaining units in existing projects. At the end of 2021, MK had 18 landed property projects, with remaining units worth around THB5.3 billion (including both built and un-built units).

MK’s strategy to focus more on the property-for-rent business should help improve its earnings stability in the long run. However, its wellness business is likely to remain under pressure from the ongoing COVID-19 situation while its “RAKxa” brand is still new to the market. Our base case expects revenue from the wellness business to be in the THB60-THB100 million range in 2022, increasing to THB200-THB300 million per annum in the following years.

Rising contribution from IE business

MK's IE business is operated under Prospect Development Co.,Ltd (PD). PD's assets comprise warehouses and ready-built factories (RBFs) located on Bangna-Trad Km. 23, Bangna-Trad Km. 19 and Theparak Roads. In addition, PD has joined Sansiri PLC (SIRI) to set up BFTZ Bangpakong Co.Ltd (BFTZB) to develop industrial property for rent in Chachoengsao province. The total leasable area of BFTZB will be around 200,000 square meters (sq.m.) with an expected investment cost of around THB8.2 billion. PD also set up a joint venture (JV) with Finansia PLC (FNS), BFTZ Wangnoi Co.Ltd. (BFTZW), to develop warehouse for rent in Ayudhya province. The total leasable area of BFTZW will be around 112,600 sq.m., with a total investment cost of around THB2.3 billion.

As of December 2021, the total leasable area under PD stood at 162,612 sq.m. The average occupancy rate in 2021 was 88% and the average rental rate was 177 THB/sq.m./month. In 2021, the revenue and EBITDA contributions from PD were THB334 million and THB227 million, respectively. Looking forward, PD plans to develop and maintain leasable area of 200,000 sq.m. to generate recurring income. Excess rental space and projects under JVs will be sold to Prospect Logistics and Industrial Freehold and Leasehold Real Estate Investment Trust (PROSPECT) for capital gains. PD would also gain a property management fee from PROSPECT. We forecast MK's revenues from IE business to be THB480-THB550 million per annum in 2022-2024 with EBITDA margin (excluding sales of assets to PROSPECT) around 67%.

Plan to divest assets to improve capital structure

We expect MK's leverage to remain high as a result of low earnings and sizable capital spending on the IE business. Capital expenditure for its own IE during 2022-2023 will total THB1.95 billion while expenditure for the construction of two warehouses under JVs will be around THB830 million in 2022 and THB900 million to THB1.1 billion per annum in 2023-2024. However, the company plans to alleviate its debt burden by divesting some assets and some land plots. PD also aims to sell IE spaces to PROSPECT at least 40,000 sq.m. annually.

Under TRIS Rating's base case, MK's FFO to debt ratio is expected to remain negative this year and improve to 4.8% in 2023, and 7.5% in 2024. Its debt to capitalization ratio is expected to reach 64% in 2022 and gradually decline to below 60% from 2023 onwards. As of December 2021, the ratio was 63%. The financial covenants on MK's debt obligations require the company to keep its net interest-bearing debt to equity ratio below 2 times. The ratio at the end of December 2021 was 1.6 times. The company should not have any problems complying with the financial covenants over the next 12 months.

At the end of December 2021, MK had debts of THB9.7 billion, comprising THB1.33 billion in bills of exchange (B/Es), THB6.6 billion in debentures, and THB1.77 billion in bank borrowings. MK's priority debt to total debt ratio was 28%, less than our 50% threshold, thus we view that MK's unsecured creditors are not significantly disadvantaged to its priority debt holders with respect to the priority of claims against the company's assets.

Tight liquidity

We assess MK's liquidity to be tight but should be manageable. As of December 2021, the company had debts of THB4.72 billion coming due in the next 12 months, comprising THB1.33 billion B/Es, THB3.14 billion debentures, THB197 million project loans, and THB50 million short-term loans. MK plans to refinance the maturing debentures with new debenture issues and to rollover its B/Es.

MK's sources of liquidity as of December 2021 comprised cash on hand of around THB194 million, investments in fixed-income fund of THB300 million, and undrawn committed credit facilities of around THB325 million. MK also has unencumbered assets worth THB1.9 billion, which can be sold or pledged as collateral for new credit facilities, if needed. In addition, FNS, the major shareholder of MK, has prepared back-up facilities of THB500 million to support MK's liquidity.

BASE-CASE ASSUMPTIONS

- Operating revenues to range from THB2.2-THB3.1 billion per annum over the next three years.
- No new project launches and land acquisition for the residential property business over the next three years.
- Capital expenditure in the industrial property for rent business of THB1.75 billion in 2022 and THB192 million in 2023.
- Investment in two JV projects of around THB830 million to THB1.1 billion per annum over the next three years.

RATING OUTLOOK

The "negative" outlook reflects our concerns over MK's weak operating performance in residential property and wellness businesses, while its financial leverage remains high. In addition, the company's financial profile could further deteriorate if the company fails to sell some assets as planned.

RATING SENSITIVITIES

We could revise MK’s outlook to “stable” if there are signs of improvement in its operations and financial profile, such that the ratio of FFO to debt stays around 5%. In contrast, we would revise the rating downward if its operating performance and/or financial profile deteriorate from our base-case forecast.

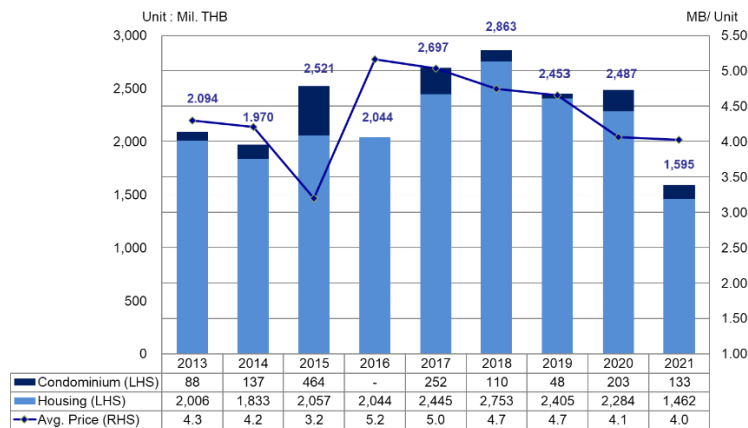
COMPANY OVERVIEW

MK was founded in 1973 by Mr. Chuan Tangmatitham and listed on the Stock Exchange of Thailand (SET) in 1990. The Tangmatitham family was MK’s major shareholder, before it sold almost its entire stake in the company to Mr. Suthep Wongvorazathe in June 2015. Mr. Suthep consequently became the major shareholder of the company, holding a 20.64% stake in MK as of September 2015. However, as MK later acquired 100% of the equity of Prospect Development Co., Ltd. (PD), partly through a share swap, Mr. Suthep’s stake in MK was diluted to 17.9% as of December 2015. The existing shareholders of PD then held 13.3% of MK with Finansa PLC, the major shareholder of PD, holding 7.15% of MK. New top managers were put in place in 2015, most with a background in the financial services industry. As of December 2021, FNS and Mr. Suthep were the major shareholders of MK, holding 31.5% and 5.5% stakes, respectively.

MK focuses on developing low-rise residential property projects, with prices ranging between THB3-THB6 million per unit, under the “Chuan Chuen” brand. Most of its products are semi-prebuilt or prebuilt single detached houses (SDHs), semi-detached houses (semi-DHs), and townhouses (THs). Apart from the residential property business, MK has expanded into the recurring income business, comprising the industrial estate for rent business as well as the wellness business, as part of its strategic diversification. MK’s revenue contributions from residential sales and from the recurring income businesses were 82% and 18% of total revenue, respectively, in 2021.

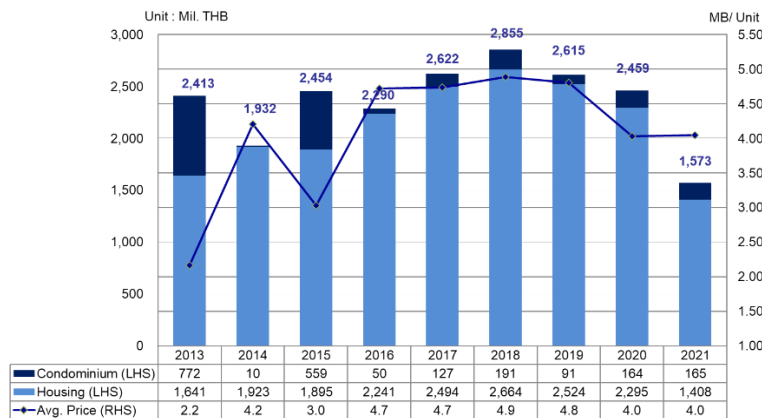
KEY OPERATING PERFORMANCE

Chart 1: Presales

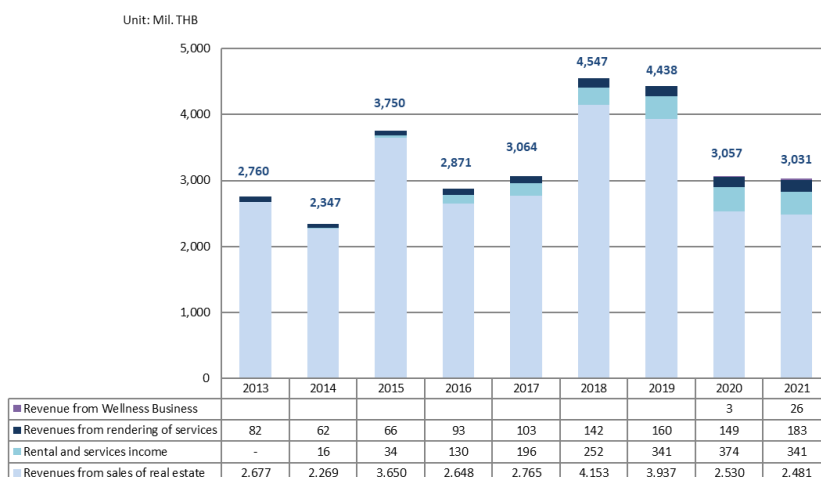


Source: MK

Chart 2: Transfers



Source: MK

Chart 3: Revenue Breakdown


Source: MK

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS*

Unit: Mil. THB

	-----Year Ended 31 December-----				
	2021	2020	2019	2018	2017
Total operating revenues	3,031	3,057	4,438	4,547	3,064
Earnings before interest and taxes (EBIT)	(53)	413	626	681	601
Earnings before interest, taxes, depreciation, and amortization (EBITDA)	243	668	838	869	736
Funds from operations (FFO)	(247)	229	432	469	387
Adjusted interest expense	489	398	350	320	262
Real estate development investments	4,601	6,143	6,164	7,149	9,941
Total assets	19,041	17,985	16,707	15,727	14,180
Adjusted debt	11,049	9,827	8,551	8,007	6,756
Adjusted equity	6,468	6,641	6,795	6,646	6,668
Adjusted Ratios					
EBITDA margin (%)	8.00	21.84	18.89	19.11	24.02
Pretax return on permanent capital (%)	(0.30)	2.51	4.05	4.77	4.49
EBITDA interest coverage (times)	0.50	1.68	2.39	2.71	2.81
Debt to EBITDA (times)	45.56	14.72	10.20	9.22	9.18
FFO to debt (%)	(2.23)	2.33	5.05	5.86	5.73
Debt to capitalization (%)	63.07	59.67	55.72	54.64	50.33

* Consolidated financial statements

RELATED CRITERIA

- Key Financial Ratio and Adjustments for Corporate Issuers, 11 January 2022
- Rating Methodology – Corporate, 26 July 2019

M.K. Real Estate Development PLC (MK)

Company Rating:	BBB-
Rating Outlook:	Negative

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