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AREEYA PROPERTY PLC

No. 2/2018 4 January 2018

Company Rating: BB

Outlook: Stable

Company Rating History:

Date	Rating	Outlook/Alert
30/12/16	BB+	Negative
13/01/15	BB+	Stable
10/01/14	BBB-	Negative
13/03/13	BBB-	Stable

Contacts:

Rapeepol Mahapant
Rapeepol@trisrating.com

Jutamas Bunyawanichkul
jutamas@trisrating.com

Auyporn Vachirakanjanaporn
auyporn@trisrating.com

Suchada Pantu, Ph. D.
suchada@trisrating.com

WWW.TRISRATING.COM

Rating Rationale

TRIS Rating downgrades the company rating of Areeya Property PLC (Areeya) to “BB” from “BB+”. The rating downgrade reflects a level of financial leverage that remains high and its tightened liquidity profile. Considering the company’s small capital base, the plans to launch a few large condominium projects over the next 2-3 years will keep the total debt to capitalization ratio higher than 70%.

The rating continues to reflect Areeya’s acceptable track record in the middle-income segment of the residential property development industry, small revenue base, and volatile operating results. In addition, the high household debt level nationwide and the cyclical and competitive nature of the property development industry remain rating concerns.

Areeya was established by the Laohapoonrungsee family in 2000 and listed on the Stock Exchange of Thailand (SET) in April 2004. The Laohapoonrungsee family has been the company’s major shareholders since inception, owning a 54% stake as of September 2017. Mr. Wisit Laohapoonrungsee remains Areeya’s chairman and chief executive officer (CEO).

Areeya offers a wide range of residential property products including single detached houses (SDHs), semi-detached houses (semi-DHs), townhouses, and condominiums. Its products target the middle-income segment. Townhouses are the company’s biggest product, contributing more than half of revenue.

As of September 2017, Areeya had about 35 active projects. The value of the unsold units, across all of its active projects, was about Bt14,700 million. The largest portion (40%) of the value was in condominium projects, with 38% in townhouse projects, and 22% in SDH projects. Areeya’s backlog stood at about Bt3,100 million as of September 2017. Nearly 60% of the value of the backlog was condominium projects.

Areeya’s revenue base is rather small, compared with other property developers rated by TRIS Rating. Revenue from the property development segment has ranged from Bt2,000-Bt5,000 million per year over the past few years. Fixed operating expenses as a percentage of revenue, a measure of operating leverage, was higher than many peer companies. High operating leverage means volatile operating results and low profitability.

Revenue in the first nine months of 2017 was flat year-on-year (y-o-y) at Bt3,595 million. Similar to other residential developers targeting the middle-to-low income segment, Areeya struggled with higher rejection rates for mortgage loans. The high level of household debt nationwide lingered on. In addition, banks implemented more stringent lending criteria. As a result, purchasing power of prospective property buyers declined.

Profitability had been improving over the last couple of years, but Areeya has lost momentum. Operating profit before depreciation and amortization as a percentage of sales (the operating margin) slid to 7.8% in the first nine months of 2017, from 12.9% in 2016. The decrease was due to a significant rise in marketing expenses. Rising competition pressured the company to offer more sales promotions. Going forward, TRIS Rating forecasts profitability will recover as revenue is expected to rise. TRIS Rating assumes the operating margin will rise to about 8% over the next three years. However, intense competition and weak purchasing power of property buyers will challenge any attempt to boost sales.

Financial leverage remained high because inventory was slow moving, particularly the inventory of condominium units. The total debt to capitalization ratio (including capitalized annual leases) has held at above 70% since 2014. As of September 2017, the net interest-bearing debt to equity ratio was 2.7 times, nearly the maximum level of 3 times stated in the terms of the bond indenture. In the coming years, the level of financial leverage is expected to remain high since the company plans to launch three condominium projects worth around Bt15,000 million. The high level of leverage raises concerns over the company's ability to comply with its bond covenants. The total debt to capitalization ratio (including capitalized annual leases) will likely reach 75% within the next three years, given TRIS Rating's base-case forecast. The net interest-bearing debt to equity ratio may rise to 2.9 times. The level of financial leverage could be lower if Areeya can speed up the sales of its completed condominium units or increase its base of equity capital.

Cash flow protection declined recently as profitability fell. The ratio of funds from operations (FFO) to total debt decreased to 1.9% (annualized, from the trailing 12 months) in the first nine months of 2017, from above 3% during 2015 and 2016. The earnings before interest, tax, depreciation, and amortization (EBITDA) interest coverage ratio fell to about 1 times, from 1.3-1.5 times during 2015 and 2016. However, cash flow protection should improve gradually as profitability improves. TRIS Rating expects the FFO to total debt ratio will rise to 2%-4% and the EBITDA interest coverage ratio will rise to 1.1-1.5 times during the next three years.

Currently, Areeya uses bonds to finance the majority of its residential property projects. A bond worth about Bt1,000 million is scheduled for repayment in 2018. As of October 2017, the company had undrawn credit facilities of Bt805 million and Bt730 million in cash on hand to support liquidity. FFO in 2018, based on TRIS Rating's forecast, will be about Bt220 million. As a result, total sources of funds will be about Bt1,755 million. Areeya plans to refinance the bond coming due in 2018 with unused credit facilities from banks and/or issuances of new bonds. The new condominium projects will be funded by project loans from banks. Areeya's high financial leverage and rather low profitability has raised concerns over its refinancing risk.

Rating Outlook

The "stable" outlook reflects the expectation that Areeya will maintain its operating performance and financial position at the current levels. The rating upside is limited in the near term, considering the current financial profile. However, the rating and/or outlook could be revised upward if profitability and financial leverage improve. The total debt to capitalization ratio needs to fall below 70%, on a sustained basis. In contrast, a rating downgrade could occur if the operating performance drops further or if the capital structure worsens more than expectations.

Areeya Property PLC (Areeya)

Company Rating:	BB
Rating Outlook:	Stable

Financial Statistics and Key Financial Ratios *

Unit: Bt million

		------------------ Year Ended 31 December --------------			
	Jan-Sep *** 2017	2016 ***	2015 ***	2014 ***	2013 ***
Revenue	3,595	4,647	5,401	2,438	1,763
Gross interest expense	441	517	486	408	295
Net income from operations	79	303	243	(21)	14
Funds from operations (FFO)	90	410	290	28	29
Inventory investment	405	(139)	(710)	(1,853)	(888)
Total assets	13,457	13,516	12,861	11,957	8,988
Total debts	9,225	9,419	8,945	8,331	5,677
Shareholders' equity	3,356	3,314	3,090	2,874	2,859
Operating income before depreciation and amortization as % of sales	7.85	12.87	8.54	4.95	5.82
Pretax return on permanent capital (%)	3.45 **	4.98	3.99	1.41	1.55
Earnings before interest, tax, depreciation, and amortization (EBITDA) interest coverage (times	0.98	1.49	1.25	0.55	0.61
FFO/total debt (%)	1.94 **	4.20	3.16	0.32	0.47
Total debt/capitalization (%)	74.03	74.66	74.84	75.29	68.05
Total debt/capitalization (%) ****	73.33	73.97	74.32	74.35	66.51

* *Consolidated financial statements*
** *Annualized with trailing 12 months*
*** *Operating lease adjusted since 2012*
**** *Excluding capitalized annual leases*

TRIS Rating Co., Ltd.
Tel: 0-2098-3000 / Silom Complex Building, 24th Floor, 191 Silom Road, Bangkok 10500, Thailand www.trisrating.com