TRIS RATING
A strategic partner of S&P Global

CreditNews ข่าวเครดิต

M.K. REAL ESTATE DEVELOPMENT PLC

No. 14/2017 28 February 2017

Company Rating: BBB

Outlook: Stable

Company Rating History:

Date	Rating	Outlook/Alert
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

Contacts:

Rapeepol Mahapant
rapeepol@trisrating.com

Auyporn Vachirakanjanaporn
auyporn@trisrating.com

Jutamas Bunyawanichkul
jutamas@trisrating.com

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

WWW.TRISRATING.COM

Rating Rationale

TRIS Rating affirms the company rating of M.K. Real Estate Development PLC (MK) at "BBB". The rating reflects MK's acceptable brand recognition in the low-rise housing segment, small revenue base, the limited track record of its top management team in the residential property industry, as well as a more aggressive financial policy. However, the company's operations continue to run smoothly after the recent change of the major shareholder and top management team. The rating also takes into consideration the high level of household debt nationwide and the cyclical and competitive nature of the residential property industry.

MK was established in 1973 and listed on the Stock Exchange of Thailand (SET) in 1990. The Tangmatitham family had been the company's major shareholder, before selling almost all its stake in MK to Mr. Suthep Wongvorazathe in June 2015. Mr. Suthep Wongvorazathe consequently became the major shareholder of MK, holding about 18% in the company as of September 2016. New top managers were put in place. Most have a background in the financial industry. MK continues to focus on developing low-rise residential property projects, with prices from Bt2-Bt5 million per unit, under the "*Chuan Chuen*" brand.

MK recently expanded into rental property. In October 2015, it completed an acquisition of 100% of the equity of Prospect Development Co., Ltd. (PD), a developer of ready-built factories (RBFs) and warehouses for rent in the Bangkok Free Trade Zone. The acquisition cost nearly Bt1,000 million. As of December 2016, PD had about 85,500 square meters (sq.m.) of rental space, with an occupancy rate (OR) of 87%. PD will require approximately Bt1,700 million to develop about 162,500 sq.m. of new rental space over the next three to four years. Rental and service income is projected to rise to Bt400-Bt500 million annually, from the current level of Bt130-Bt140 million, if all the rental space is completed.

In addition, MK purchased three land plots during 2015 and 2016 to develop a mixed-use project, on Sukhumvit 77 road, blending rental apartments and a condominium. The land cost MK about Bt3,000 million, which was a sizable amount for the company. MK sold its existing raw land, worth about Bt1,250 million, to reduce funding needs for the investment. The project has three phases. The first phase comprises five low-rise buildings, with 70 units in total. Construction costs for the first phase are estimated at about Bt600 million. MK plans to complete construction of the first phase in the third quarter of 2017. The other phases are planned for 2018-2019. The success of this project remains a challenge for the company.

As of December 2016, MK had 12 active residential property projects. The combined value of the unsold units in these projects was about Bt4,200 million. The company had a small backlog, worth about Bt270 million, because most of its products are semi-prebuilt or prebuilt single detached houses (SDHs), semi-DHs, and townhouses (THs). MK's revenue is smaller than most other developers rated by TRIS Rating. Revenue has ranged from Bt1,700-Bt2,800 million over the past five years, except in 2015 when the company sold raw land and realized about Bt1,250 million in revenue. Revenue in the first nine months of 2016 was Bt1,931 million, a 2.6% year-on-year (y-o-y) drop. However, excluding the sale of raw land, revenue in the first nine months of 2016 increased by 41.5% y-o-y. Over the next three years, TRIS Rating forecasts MK's revenue will grow from about Bt2,600 million in

2016 to reach Bt4,000 million in 2019, mostly driven by the sales of units in the mixed-use project. Revenue from its rental property business is expected to contribute 7%-10% to total revenue, rising from about 5% in the first nine months of 2016.

Profitability has improved recently. The operating margin, as measured by operating income before depreciation and amortization as a percentage of sales, rose to 19.4% in the first nine months of 2016, from 15.7% in 2015. In 2015, MK reduced inventory by offering sales promotions, squeezing the gross margin for the year. Over the next three years, TRIS Rating forecasts the operating margin will stay above 19%.

Financial policy is more aggressive now after the recent change of the major shareholder and top management team. The recent acquisition of PD and the purchase of three land plots on Sukhumvit 77 road significantly raised the debt to capitalization ratio to 47.4% as of September of 2016, compared with the past level of about 20%. Over the next three years, MK will require a significant amount of investment as the rental property segment expands. MK plans to dispose some raw land to reduce its funding needs. The managers intend to keep the debt to total capitalization ratio at around 50%. A further rise in leverage, without the commensurate returns, will affect the company's rating negatively. In contrast, a successful diversification into the rental property business will be a plus for MK.

Liquidity is tightening as leverage rises. The fund from operation (FFO) to total debt ratio decreased to 7.7% (annualized, from the trailing 12 months) in the first nine months of 2016, from the past level of more than 15%. The FFO to total debt ratio is projected to bottom out in 2017, before rising to 8%-10% during 2018-2019 when revenue grows significantly. MK has debts coming due in 2017, worth about Bt2,300 million, mostly are bills of exchange (B/Es). FFO in 2017 is projected to be Bt400-Bt500 million. MK has undrawn committed credit facilities of about Bt600 million, plus cash and marketable securities of about Bt500 million. As a result, sources of cash will total approximately Bt1,550 million. This means the company has to refinance some of the coming debts due in the year.

Rating Outlook

The "stable" outlook reflects the expectation that MK's operating performance will remain at the current level. The company is also expected to maintain the debt to capitalization ratio around 50% over the next three years. MK's rating upside is limited while it is investing. The rating and/or outlook could be revised upward if the company successfully diversifies into the rental property business, while meeting the financial leverage target. In contrast, the rating and/or outlook could be downgraded if the operating performance and financial position drop significantly below expectations.

M.K. Real Estate Development PLC (MK)

Company Rating:	BBB
Rating Outlook:	Stable

Financial Statistics and Key Financial Ratios*

Unit: Bt million

	Jan-Sep 2016	------------------------ Year Ended 31 December ---------------------- 2015	2014	2013	2012	2011
Revenue	1,931	3,750	2,347	2,760	1,724	1,673
Gross interest expense	119	98	50	67	78	55
Net income from operations	194	427	443	429	260	234
Funds from operations (FFO)	238	480	478	495	278	212
Inventory investment	(1,062)	357	(624)	761	(527)	(471)
Total assets	13,200	11,678	7,361	6,783	7,359	6,773
Total debts	5,878	4,239	1,297	920	1,768	1,267
Shareholders' equity	6,530	6,638	5,470	5,280	5,007	4,901
Operating income before depreciation and amortization as % of sales	19.39	15.73	24.00	19.73	18.44	19.62
Pretax return on permanent capital (%)	5.07 **	6.59	8.58	8.39	5.28	5.66
Earnings before interest, tax, depreciation, and amortization (EBITDA) interest coverage (times)	4.11	7.01	12.43	9.22	5.14	7.26
FFO/total debt (%)	7.74 **	11.32	36.88	53.86	15.75	16.72
Total debt/capitalization (%)	47.37	38.98	19.17	14.83	26.10	20.54

* *Consolidated financial statements*
** *Annualized with trailing 12 months*

TRIS Rating Co., Ltd.
Tel: 0-2231-3011 ext 500 / Silom Complex Building, 24th Floor, 191 Silom Road, Bangkok 10500, Thailand www.trisrating.com