

CHARN ISSARA DEVELOPMENT PLC

No. 87/2022
30 May 2022

CORPORATES

Company Rating: BB
Outlook: Stable

Last Review Date: 30/04/21

Company Rating History:

Date	Rating	Outlook/Alert
30/04/21	BB	Stable
09/04/20	BB+	Negative
23/04/18	BB+	Stable
16/08/13	BBB-	Stable

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RATIONALE

TRIS Rating affirms the company rating on Charn Issara Development PLC (CI) at “BB”, with a “stable” rating outlook. The rating reflects CI’s small and volatile revenue base, acceptable market presence, high financial leverage, and relatively tight but manageable liquidity. The rating also takes into consideration our concerns over the country’s high level of household debt and rising inflation which may impact the purchasing power of homebuyers and raise the costs of property developers in the short to medium term.

KEY RATING CONSIDERATIONS

Revenue base remains small and volatile

CI’s business scale remains modest, compared with other rated real estate developers. Its revenue base has ranged from THB1.3-THB2.0 billion per annum over the past three years. The company ended 2021 with an operating revenue of THB2.0 billion, accounting only 0.7% of the total revenues generated by 24 developers rated by TRIS Rating. Real estate sales remain the company’s major source of revenue, contributing 73% of total operating revenue, while the revenue contributions from hotel operations and other rental and services were 17% and 3%, respectively.

CI’s revenues from real estate sales are relatively volatile and concentrated in very few projects. As of March 2022, CI had 12 active residential property projects, located in Bangkok and major tourist destinations, notably Cha-am, Hua Hin, and Phuket. The value of unsold units (both built and un-built units) was THB7.5 billion, comprising condominiums (50%), single detached houses (SDH) (31%), and residential villas (19%). The company’s backlog stood at THB2.2 billion at the end of March 2022, of which THB800 million will be recognized as revenues in 2022. The remaining backlog will be gradually realized as revenue once the condominiums under constructions are completed in 2023-2024.

Acceptable market presence in the middle- to high-end segments

We maintain our view that CI has decent brand recognition in residential property and hotels in the middle- to high-end customer segment. Its products are well-accepted for quality and style. CI’s residential properties are developed under the “Issara” and “Baan Issara” brands. Its housing products cover the middle to luxury segment, with units priced above THB50 million accounting for almost 50% of the value of its remaining housing projects as of March 2022.

CI’s luxury residential villas and hotels are also well-recognized with mixed-use projects located in prominent tourist destinations, such as Cha Am, Hua Hin, Phuket, and Phang Nga. In our view, the development of mixed-use projects helps enhance the value of CI’s housing products.

Operating performance to gradually recover

CI’s operating performance has been relatively weak and highly volatile over the past few years. The prolonged COVID-19 pandemic negatively affected both its residential property and hotel businesses. In addition, the company had to postpone sales of its assets to the Sri Panwa Hospitality Real Estate Investment Trust (SRIPANWA) to 2023. As a result, the company may continue to report a loss this year. Nonetheless, our base case expects the company’s bottom line to turn positive from 2023 onwards.

In our base case forecast, we expect CI's real estate and hotel business to gradually improve with operating revenue ranging from THB2.4-THB4.0 billion per annum in 2022-2024. The backlog on its SDHs should be transferred this year while its two new condominiums, "The Issara Sathorn" and "Sasara", are expected to be completed and ready to transfer in 2023-2024. For its hotel business, an increase in the number of room keys and an improvement in occupancy rates following the lifting of travel restrictions should help enhance its rental and service income over the next few years.

In terms of profitability, we expect the company's earnings before interest, taxes, depreciation, and amortization (EBITDA) margin to remain under pressure in 2022, weighed down by the slump in the hotel business. As we anticipate the earnings capacity of both real estate sales and hotel operations to improve gradually over the next three years, we project the gross profit margin to increase from 22%-24% in 2022-2023 to around 28% in 2024. The EBITDA margin is likely to range from 14%-25% over the forecast period. The company's plan to sell its assets to SRIPANWA should also provide an extraordinary uplift to its EBITDA margin in 2023. Assets slated to be sold include hotel units in the "Baba Beach Club Hua Hin" worth THB1.5 billion, hotel units in the "Baba Beach Club Phang Nga" worth THB500 million, and the convention hall of "Sri Panwa Hotel" worth THB1 billion.

Heightened concerns over household debt and rising inflation

As of December 2021, Thailand's household debt peaked at THB14.58 trillion. The household debt to gross domestic product (GDP) ratio stood at 90.12%, increasing slightly from 89.66% at the end of 2020. The relatively slow pace of economic recovery has caused the ratio to hang at a high level. The Thai GDP dropped by 6.2% year-on-year (y-o-y) in 2020 and grew by only 1.6% y-o-y in 2021. We expect the GDP to grow by 2%-3% y-o-y. Thus, assuming household debt stays at the same level, the household debt to GDP ratio should remain at around 87%-88% in 2022. The relatively high household debt level will impact residential property sales, especially in the lower-priced housing segment where bank rejection rates are high. However, in our view, CI's focus on the upscale segment helps alleviate the negative impacts of high household debt level.

However, rising inflation rates since the last quarter of 2021 pose a threat to both developers and homebuyers. High inflation rates will push up development and funding costs for developers while lowering the purchasing power of homebuyers. Soaring inflation will also impact the prices of construction materials and labor costs. Thus, developers' profit margins could decline if they are unable to pass the rising costs through to homebuyers.

Financial leverage to remain high

We expect CI's financial leverage to remain high over the next few years with a projected debt to capitalization ratio of around 68%-76%. This is based on our assumptions that the company will launch new residential projects worth around THB1-THB2 billion per annum during the forecast period. The budget for land acquisition and hotel operations is expected to be THB300-THB500 million per annum over the next three years. Assuming the company can transfer its housing units and sell its assets to SRIPANWA as planned, its funds from operations (FFO) to total debt ratio should improve from a slight negative figure in 2022 to around 8%-10% in 2023 and 2024.

The financial covenants on CI's debt obligations require the company to maintain its ratio of interest-bearing debt to equity below 3.75 times. At the end of March 2022, the ratio was 3.18 times. We expect the company should have no problem complying with the financial covenant over the next 12 months.

Manageable liquidity

We expect CI's liquidity to remain manageable over the next 12 months. As of December 2021, the company had maturing debt over the next 12 months totaling THB1.1 billion, comprising THB800 million in debentures, THB229 million in project loans, THB57 million in long-term loans, and THB20 million in short-term loans from financial institutions. At the end of December 2021, CI's sources of liquidity included cash on hand of THB336 million, short-term investments of THB562 million, unused committed credit facilities of THB1.7 billion, and unused uncommitted facilities of THB318 million. The company also has a 16% stake in a land plot held by its affiliate, International Resource Development Co., Ltd., which can be used as another source of funds. The appraised value of the land plot was around THB2.5 billion. CI usually refinances its matured debentures with new debenture issuances. Project loans are normally repaid with the proceeds from the underlying projects' unit transfers.

At the end of December 2021, CI had total debt excluding lease liabilities of THB4.7 billion. The company's priority debt, including secured debts at the company and its subsidiaries, was THB3.6 billion, which translates to a priority debt to total debt ratio of 76%. As the priority debt to total debt ratio exceeds the 50% threshold according to TRIS Rating's "Issue Rating Criteria", we view that the company's unsecured creditors are significantly disadvantaged to its priority debt holders with respect to the priority of claims against the company's assets.

BASE-CASE ASSUMPTIONS

These are the key assumptions in TRIS Rating's base-case forecast for CI's operations during 2022-2024:

- Operating revenues to range from THB2.4-THB4.0 billion per annum with contributions from hotel operations and the office rental segment to range from THB600-THB900 million per annum.
- Total capital expenditure for hotels and land acquisitions to be around THB300-THB500 million per annum.
- EBITDA margin to be around 14%-25%.

RATING OUTLOOK

The "stable" outlook reflects the expectation that CI's financial profile will improve gradually, with a debt to capitalization ratio of 70%-75% and the company's EBITDA margin holding at 10%-15% for the next three years.

RATING SENSITIVITIES

CI's ratings and/or outlook could be revised downward should its operating performance and/or financial profile deteriorate further from the current level. On the contrary, the outlook could be revised upward if the company demonstrates significant and sustainable improvements in its operating performance.

COMPANY OVERVIEW

CI was established in 1989 by the Issara family. CI became a public company in June 2002 and was listed on the Stock Exchange of Thailand (SET) in December 2002. The Issara family has been the company's major shareholder since its inception. As of March 2022, the Issara family held a 44% stake in the company.

CI's residential property products target the middle- to high-income segments. At the end of March 2022, the residential property portfolio comprised condominiums (50% of the total remaining value of the project portfolio), single detached houses (SDH) (31%), and residential villas (19%). CI's existing residential projects are located in Phetchaburi (24% of the total remaining value of the project portfolio), Phuket (18%), Bangkok (49%), Nakorn Ratchasima (3%), and Chiang Mai (6%).

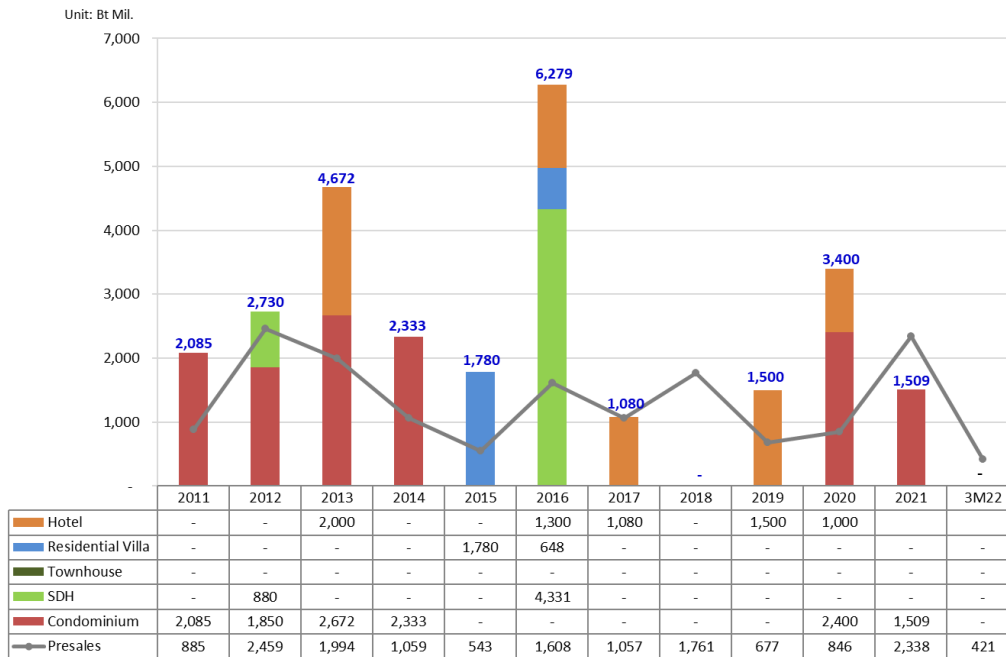
CI started to develop luxury residences for sale and opened its first boutique hotel, Sri Panwa, in Phuket in 2003. The Sri Panwa Hotel started operations in 2006. The company sold the Sri Panwa Hotel to Sri Panwa Hotel Property Fund (SPWPF) in 2013 and simultaneously purchased 30% of SPWPF. In 2016, SPWPF converted from a property fund to a REIT named SRIPANWA. Currently, CI holds 19.4% of SRIPANWA. The company also owns 17.6% of Bangkok Commercial Property (BKKCP), a property fund that owns two office buildings, "Charn Issara Tower I" and "Charn Issara Tower II". CI manages these two office buildings for the fund. In addition, the company owns 3,578 square meters of retail space in these two buildings.

In 2015, CI developed its second mixed-use project in Phang Nga under an 86:14 joint venture (JV) with Junfa Real Estate Co., Ltd., a Chinese operator. The project included 24 villas for sale and a boutique hotel under the brand "Baba Beach".

In 2016, CI formed a 50:25:25 JV with Saha Pathanapibul PLC (SPC) and I.C.C. International PLC (ICC) to develop another mixed-use project under the brand "Baba Beach" in Cha-am district, Phetchaburi. In 2021, CI opened "Habita Seaview", an extension of Baba Beach Hua Hin Hotel. The company also plans to open phase 3 of Baba Beach Hua Hin residential villa in 2022.

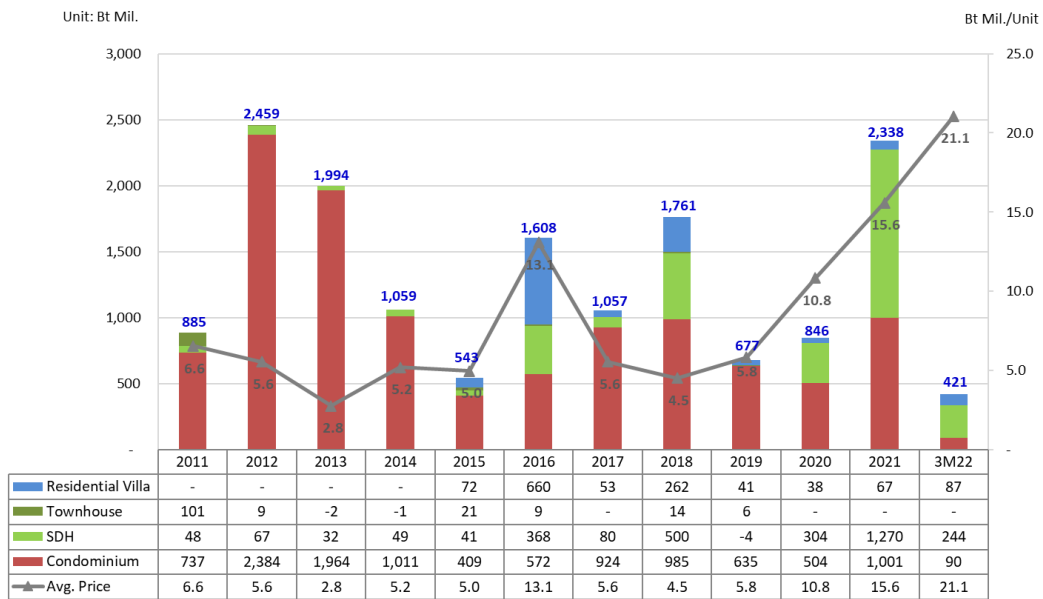
KEY OPERATING PERFORMANCE

Chart 1: Residential and Hotel Project Launches



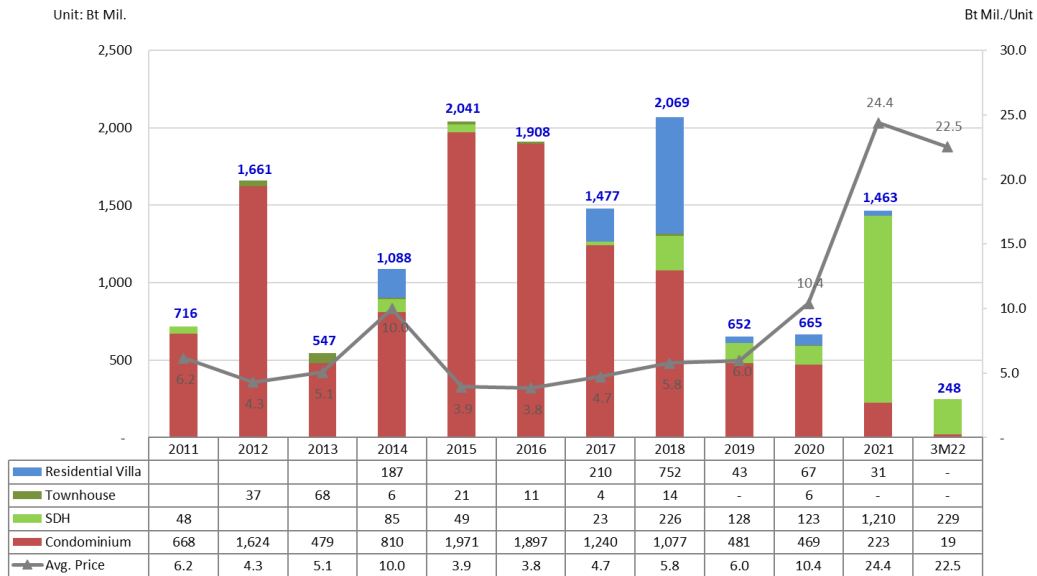
Source: CI

Chart 2: Presales Performance



Source: CI

Chart 3: Transfers Performance



Source: CI

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS*

Unit: Mil. THB

	Jan-Mar **	-----Year Ended 31 December -----			
	2022	2021	2020	2019	2018
Total operating revenues	423	2,001	1,348	1,501	2,950
Earnings before interest and taxes (EBIT)	(43)	25	(176)	(276)	484
Earnings before interest, taxes, depreciation, and amortization (EBITDA)	37	298	101	1	615
Funds from operations (FFO)	(37)	(26)	(230)	(385)	285
Adjusted interest expense	74	324	331	387	294
Real estate development investments	5,113	5,120	5,588	4,939	4,344
Total assets	10,721	10,199	10,805	8,681	7,767
Adjusted debt	6,351	6,293	6,868	5,628	5,275
Adjusted equity	2,276	2,402	2,438	2,949	2,798
Adjusted Ratios					
EBITDA margin (%)	8.63	14.88	7.49	0.09	20.83
Pretax return on permanent capital (%)	(0.47)	0.26	(1.80)	(2.97)	5.50
EBITDA interest coverage (times)	0.49	0.92	0.31	0.00	2.09
Debt to EBITDA (times)	26.41	21.13	68.05	4,067.48	8.58
FFO to debt (%)	(1.15)	(0.42)	(3.35)	(6.84)	5.41
Debt to capitalization (%)	73.62	72.37	73.80	65.62	65.34

* Consolidated financial statements

** Annualized from the trailing 12 months

RELATED CRITERIA

- Key Financial Ratio and Adjustments for Corporate Issuers, 11 January 2022
- Issue Rating Criteria, 15 June 2021
- Rating Methodology – Corporate, 26 July 2019

Charn Issara Development PLC (CI)

Company Rating:	BB
Rating Outlook:	Stable

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