

# HEMARAJ LEASEHOLD REAL ESTATE INVESTMENT TRUST

No. 134/2021  
30 August 2021

## CORPORATES

**Company Rating:** BBB+  
**Outlook:** Stable

**Last Review Date:** 14/08/20

### Company Rating History:

Date	Rating	Outlook/Alert
09/10/18	BBB+	Stable

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## RATIONALE

TRIS Rating affirms the company rating on Hemaraj Leasehold Real Estate Investment Trust (HREIT or trust) at “BBB+” with a “stable” outlook. The rating reflects the trust’s satisfactory operating performance, rather small size, tenant concentration, and its moderate financial leverage. The rating also takes into consideration our concerns over the resurgence of Coronavirus Disease 2019 (COVID-19) in the country, which may put pressure on the demand and renewal rate for industrial properties.

## KEY RATING CONSIDERATIONS

### Satisfactory occupancy rate

We expect HREIT to maintain its satisfactory occupancy rate (OR) in the medium term, given the strategic locations of HREIT’s properties as well as asset enhancement supported by its sponsor.

The trust’s properties are located in key industrial and logistics areas in Thailand, comprising the Eastern Economic Corridor (EEC) (90%) and Saraburi province (10%). Based on occupied area, the trust’s tenants are mainly engaged in the consumer products industry (30%), automotive industry (29%), and logistics providers (19%).

Despite the impact of the COVID-19 pandemic, the trust was able to keep its OR (exclusive of the yield-enhancement from the sponsor’s undertaking) at around 90%-95% during 2020 through the first half of 2021. Trade tensions between the United States (US) and China triggered a rise in demand for industrial properties resulting from the relocation of some manufacturing bases and supply chains from China to Thailand. The proportion of Chinese tenants jumped from 22% in 2019, to 27% in 2020 and 33% in the first half of 2021. In addition, strong recoveries in developed economies after the rollouts of COVID-19 vaccines benefited HREIT’s export-oriented tenants. However, we see continued risk as the ongoing COVID-19 pandemic and slow vaccination rate in Thailand may put pressure on the demand and renewal rate for industrial properties. In addition, new demand from foreign investors remains slack due to the ongoing travel restrictions. The growth in new demand from foreign investors will rely largely on the vaccination rate in Thailand.

The acquisition of new assets with high ORs and undertaking scheme supported by the trust’s sponsor, WHA Industrial Development PLC (WHAID), should also help maintain portfolio performance at the current level. In mid-December 2020, HREIT acquired new assets worth THB1.43 billion from its sponsor. We expect the trust to invest around THB1.5 billion per annum on new rental assets during 2022-2023. As a result, we expect OR (with undertaking) to remain in the 90%-91% range over the next three years. Thus, HREIT’s revenue is forecast to at around THB760-THB910 million per annum during 2021-2023.

### Maintaining favorable earnings amid uncertainty

HREIT’s revenue declined 11% year-on-year (y-o-y) to THB686 million in 2020, mainly because the undertaking agreement with the sponsor, covering 78.6% of total leasable area, expired in November 2019. In addition, extra spending in selling, general, and administrative expenses (SG&A), which were refinance-related expenses and marketing expenses from capital-raising

activities, led to a decline in margin. As a result, the trust's earnings before interest, taxes, depreciation, and amortization (EBITDA) margin in 2020 declined to 87%, compared with 90%-91% during 2017-2019. Its EBITDA stood at THB597 million in 2020.

Normally, the trust's sponsor commits to pay rental income to the trust for the first three years for vacant property space in every new acquisition in order to enhance OR to 100%, and further commits to make up any shortfall if the rental rates offered to tenants fall below a guaranteed rental rate. Undertaking agreements from the sponsor, covering 14% and 4% of total leasable area as of June 2021, expire in January and December 2021, respectively. We do not expect the expiration to have a material impact on performance due to the trust's high ORs.

Going forward, we expect HREIT's EBITDA margin to hold in the 85%-89% range during 2021-2023. Thus, EBITDA should be around THB680-THB770 million during the same period. HREIT's EBITDA interest coverage ratio is expected to improve to 5.5-7 times over the next three years, from around 5 times in 2020, given that the trust refinanced its bank loans with lower interest loans.

### **Comparatively small business size**

HREIT is significantly smaller than the other industrial REITs rated by TRIS Rating. As of June 2021, HREIT held investment properties worth THB11.19 billion, while Frasers Property Thailand Industrial Freehold and Leasehold REIT (FTREIT: rated "A" by TRIS Rating) held properties valued at THB43.89 billion and WHA Premium Growth Freehold and Leasehold Real Estate Investment Trust (WHART: rated "A" by TRIS Rating) held THB39.6 billion. We view that asset size matters with respect to the ability to generate revenue. For the 12-month period of fiscal year (FY) 2020, HREIT's total revenues came to THB686 million compared with revenues of THB3.04 billion for FTREIT and THB2.55 billion for WHART. However, we believe HREIT has the potential to enlarge its asset portfolio given the support of its sponsor.

### **Exposure to portfolio concentration risk**

We view that HREIT remains exposed to tenant concentration risk. The top-ten tenants occupied 37% of the total occupied area and contributed 36% of total rental and service income in the first half of 2021. However, the tenant concentration risk is partly mitigated by the solid credit profiles of the largest tenants. We expect tenant concentration risk to gradually dissipate as asset size grows.

HREIT is also exposed to contract renewal risk. Most of HREIT's lease contracts have a three-year lease term. Of the existing contracts based on leased area at the end of June 2021, around 28% will expire in the second half of 2021, 45% in 2022, 22% in 2023, and the rest will expire thereafter. Lease contract expirations are relatively concentrated in 2021 and 2022, since the lease agreements of 10 major tenants will expire within the same period. The renewal rate in 2020 was 60%, declined from 69% in 2019. However, the trust was able to find new tenants and maintain ORs at more than 90% at the end of 2020. During the first half of 2021, the renewal rate was 58%. We expect the renewal rate in 2021 to stay above 70% as at least 80% of expired contracts in the second half of 2021 have already been renewed. The property manager normally negotiates lease renewal agreements with tenants about three to six months in advance of expiration. Thus, the trust has time to seek new tenants in the event of contract terminations.

### **Moderate financial leverage**

Under its financial policy, HREIT aims to keep its loan to fair value of total assets ratio (LTV) below 40% in the medium to long term. Over the past four years, the trust has generally funded its assets acquisitions through a combination of debt and equity with the LTV ratio in the range of 27%-34%. At the end of June 2021, the trust's LTV ratio stood at 32%.

HREIT intends to enlarge its property portfolio consistently, mainly through its sponsor. In mid-December 2020, the trust acquired THB1.43 billion in new assets using 30% debt funding, resulting in an LTV ratio of around 32% at the end of 2020. Under its growth strategy, we forecast HREIT to acquire new assets of around THB1.5 billion per annum in 2022-2023. We expect the trust to fund its future acquisitions through a combination of debt and equity. As a result, LTV is expected to remain in the 32%-33% range.

At the end of June 2021, HREIT's secured debt to fair value of total assets ratio was 32%. As the percentage of secured debt was lower than 35% of the fair market value of assets, we do not view HREIT's unsecured creditors to be significantly disadvantaged with respect to the priority of claims against assets.

### **Manageable liquidity**

We assess HREIT's liquidity as manageable over the next 12 months, given its ability to access financial markets. As of June 2021, HREIT's outstanding debt was THB3.75 billion, all of which was made up of long-term loans due to be repaid in 2023. The trust's sources of liquidity include cash on hand of THB315 million. We forecast EBITDA to stay around THB680 million over the next 12 months. HREIT's debt to EBITDA ratio is forecast to stay below 6 times and EBITDA interest coverage ratio

is expected to range from 5.5-7 times over the next three years.

The financial covenant on HREIT's loan obligations requires the trust to keep its debt to EBITDA ratio below 6.5 times, its interest-bearing debt to equity ratio below 1 times, and its LTV ratio below 50%. The ratios at the end of June 2021 were 5.6 times, 0.5 times, and 32%, respectively. We assess the trust should have no problem complying with the financial covenant over the next 12 months.

### BASE-CASE ASSUMPTIONS

- Investment assets to increase by THB1.5 billion per year during 2022-2023.
- OR (with the sponsor's undertaking) to range from 90%-91% over the next three years.
- Total revenue of THB760-THB910 million per annum during 2021-2023.
- EBITDA margin to range from 85%-89% over the next three years.

### RATING OUTLOOK

The "stable" outlook reflects our expectation that HREIT's property portfolio will continue to generate stable cash flows during 2021-2023. We also expect the trust's assets to sustain a high level of OR above 90% with sound profitability. In addition, we expect the trust will be able to keep the LTV below 40% in accordance with the trust's policy and remain in compliance with its financial covenants.

### RATING SENSITIVITIES

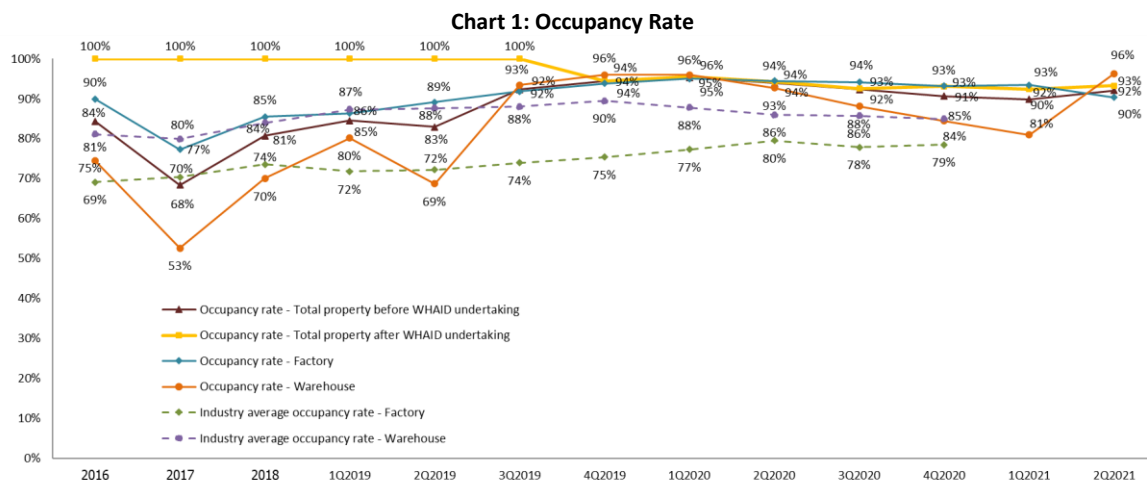
The credit rating on HREIT could come under downward pressure if the OR drops significantly below expectations and/or the trust undertakes a larger-than-expected debt-funded expansion over a prolonged period. On the other hand, the rating could be revised upward if HREIT is able to enlarge its business scale while maintaining satisfactory performance.

### COMPANY OVERVIEW

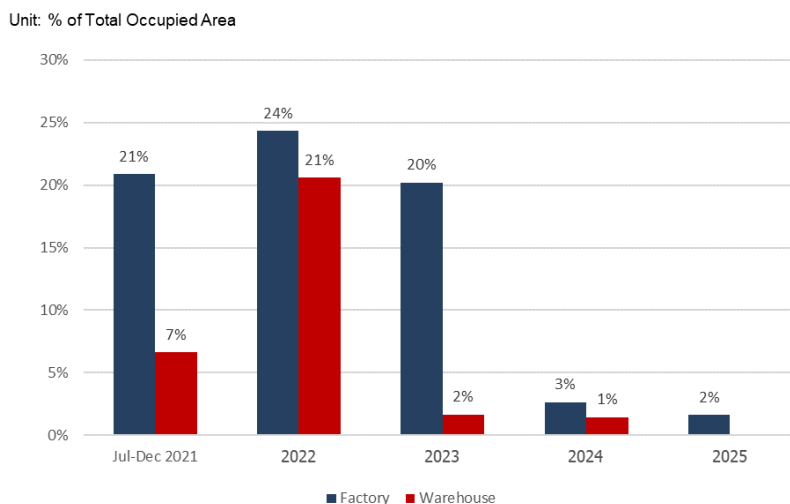
HREIT was established and listed on the Stock Exchange of Thailand (SET) in November 2016, with registered capital of THB5.69 billion. At present, WHAID holds a 15% stake in HREIT. The REIT manager of the trust is WHA Industrial REIT Management Co., Ltd. (WHAIRM) which is wholly owned by WHAID, the property manager and main sponsor of the trust. HREIT focuses on the acquisition of leasehold rights for good-quality and well-occupied industrial properties including standard warehouses and ready-built factories.

As of June 2021, the investment asset size of HREIT was valued at THB11.19 billion with total leasable area of 380,632 square meters (sq.m.). HREIT's property portfolio comprised factories (71%) and warehouses (29%) in three provinces: Chonburi, Rayong, and Saraburi. HREIT's properties are located in key industrial estates and manufacturing hubs in Thailand. About 90% of the leasable properties are located in the EEC development area.

### KEY OPERATING PERFORMANCE



Note: OR as of end of period  
Sources: HREIT and CB Richard Ellis (CBRE)

**Chart 2: Lease Expiry**


Source: HREIT

**FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS\***

Unit: Mil. THB

	Jan-Jun 2021	----- Year Ended 31 December -----			
		2020	2019	2018	2017
Total operating revenues	382	686	767	725	576
Earnings before interest and taxes (EBIT)	336	585	681	645	522
Earnings before interest, taxes, depreciation, and amortization (EBITDA)	342	597	693	655	523
Funds from operations (FFO)	290	479	556	537	426
Adjusted interest expense	52	118	137	118	97
Capital expenditures	0	1,363	0	2,091	0
Total assets	11,574	11,489	9,914	9,691	8,434
Adjusted debt	3,409	3,359	3,058	3,076	1,046
Adjusted equity	7,610	7,410	6,384	6,181	5,985
<b>Adjusted Ratios</b>					
EBITDA margin (%)	89.54	87.06	90.38	90.31	90.76
Pretax return on permanent capital (%)	5.89 **	5.62	7.12	7.27	6.40
EBITDA interest coverage (times)	6.59	5.07	5.06	5.55	5.41
Debt to EBITDA (times)	5.40 **	5.63	4.41	4.70	2.00
FFO to debt (%)	15.37 **	14.27	18.19	17.46	40.76
Debt to capitalization (%)	30.94	31.19	32.39	33.23	14.87

\* Consolidated financial statements

\*\* Annualized with trailing 12 months

**RELATED CRITERIA**

- Rating Methodology for Real Estate for Rent Companies, 15 July 2021
- Key Financial Ratios and Adjustments, 5 September 2018

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**Hemaraj Leasehold Real Estate Investment Trust (HREIT)**

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<b>Company Rating:</b>	BBB+
<b>Rating Outlook:</b>	Stable

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**TRIS Rating Co., Ltd.**

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