

CPN RETAIL GROWTH LEASEHOLD REIT

No. 143/2022
22 August 2022

CORPORATES

Company Rating:	AA
Issue Ratings:	
Senior unsecured	AA
Outlook:	Negative

Last Review Date: 04/02/22

Company Rating History:

Date	Rating	Outlook/Alert
22/07/20	AA	Negative
25/05/18	AA	Stable

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RATIONALE

TRIS Rating affirms the company rating on CPN Retail Growth Leasehold REIT (CPNREIT) and the ratings on CPNREIT's existing senior unsecured debentures at "AA", with a "negative" rating outlook. The ratings on CPNREIT and its debentures reflect the trust's high-quality assets, its predictable cash flow from contract-based rental and service income, and its conservative financial policy. The ratings also take into consideration CPNREIT's adequate liquidity and future growth opportunities, supported by assets from its sponsor, Central Pattana PLC (CPN), rated "AA/Stable".

The "negative" outlook reflects our concerns over delays in the trust's asset acquisitions and equity injections that have led to weaker-than-expected financial performance and continued high financial leverage.

KEY RATING CONSIDERATIONS

Thailand's largest REIT with high-quality assets

CPNREIT is the largest real estate investment trust (REIT) in Thailand with total investment properties worth THB76.14 billion as of June 2022. CPNREIT's real-estate portfolio consists of seven shopping malls, four office buildings, and a hotel. The properties are located in Bangkok and three provinces. The REIT has leasable area totaling 362,219 square meters (sq.m.) and 304 hotel rooms. The average occupancy rates (OR) for shopping malls and offices as of June 2022 were 94% and 85%, respectively.

Adversely affected by COVID-19 in 2021

The Coronavirus Disease 2019 (COVID-19) pandemic had a significant impact on CPNREIT's operation during 2020-2021. Shopping malls and tenant's stores were obliged to close or limit their operating hours to comply with government restrictions. To ease the hardships of tenants and to shore up occupancy rates, CPNREIT offered rental discounts of 20%-70% during 2020-2021. As a result, CPNREIT's rental and service revenues decreased to THB4.0 billion in 2020 and THB3.5 billion in 2021, from around THB5.0 billion annually during 2018-2019. Despite the setbacks, CPNREIT acquired two new shopping malls, namely Central Marina and Central Lampang from CPN in February 2021.

Office buildings contributed around 20% of CPNREIT's revenue in 2021, following the acquisition of two new properties, The 9th Towers and Unilever House, from GLAND Office Leasehold Real Estate Investment Trust (GLANDRT) in March 2020. The average OR of the trust's office buildings declined to 85% in 2021, from 90% in 2019. The decline was largely the result of the work-from-home (WFH) policy, introduced to control the spread of the disease. Some businesses have continued their WFH policies to reduce office rents and save costs even after the pandemic.

Hotels in Pattaya, which rely mainly on foreign travelers, were also affected by COVID-19. CPNREIT waived rental fees for its hotel during three quarters of 2021. The average OR dropped to 20%-25% in the first three quarters of 2021, from around 90% in 2018-2019.

Nevertheless, we expect the trust's performance to gradually improve following the government's lifting of restrictions and a general improvement in the country's COVID-19 situation from the fourth quarter of 2021 onwards.

Recovery in retail property and hotels in 2022

The retail business in Thailand began to normalize in November 2021 when the government gradually relaxed restrictions on the retail sector. With continued improvement of the COVID-19 situation in the country, we expect to see a continuous recovery of retail property in 2022. Recent customer traffic at CPNREIT's shopping malls was close to 70% of the 2019 pre-COVID-19 level. However due to continuing weak consumer spending, CPNREIT expects to continue to provide rent discounts of 5%-15% for some tenants during 2022-2023.

The country's opening, along with government stimulus measures, should help improve hotel operations in 2022. The average OR of the trust's hotel in the second quarter of 2022 was around 80%, recovering considerably from 2021. Hotel rental fees are expected to return to pre-covid level from 2023 onwards.

We forecast that the trust's rental and service income will improve to the THB5.1-THB7.5 billion per annum range during 2022-2024 while its earnings before interest, taxes, depreciation, and amortization (EBITDA) will soar to THB4.0-THB6.0 billion per annum. The projected revenue growth in 2023 and 2024 is partly derived from the contribution of new assets to be acquired during 2023-2024.

Pending assets acquisition to be executed in 2023

CPN, as a sponsor of the trust, normally adds mature properties with high OR and rental rates to the trust's portfolio. Based on the trust's original plan in late 2019, CPNREIT intended to acquire six new assets within the first half of 2020, including four shopping centers from CPN and two office buildings from GLANDRT, worth THB30.4 billion. The trust aimed to raise funds for the acquisitions using 65% equity and 35% debt. However, the COVID-19-induced risk-off sentiment in the capital market forced the trust to curtail its plans, acquiring only two office buildings from GLANDRT in March 2020 with full debt funding. The trust postponed its acquisitions of Central Marina and Central Lampang until February 2021, totally funded by equity. With the lingering COVID-19 situation and Russia-Ukraine conflicts, sentiment in the capital market remains unfavorable and the trust has postponed pending acquisitions of assets into 2023. The trust's loan-to-fair value of total assets (LTV) ratio (excluding lease liability in loans and assets) stood at 38% as of June 2022.

Our revised base-case scenario assumes the trust will acquire the new shopping centers and office buildings worth THB16.5 billion during 2023-2024. If the acquisitions go ahead as expected, the trust's leasable area will increase by 109,100 sq.m. and its annual rental income will likely rise by around THB1 billion. The growing size of the property portfolio should help boost rental income as well as diversify the trust's sources of cash flow in the future.

Leverage expected to fall

We expect the trust to improve its financial leverage by lowering its LTV ratio to a level of around 35% in 2023-2024 following the acquisition of new assets.

Our base-case scenario assumes an equity injection, totaling THB14 billion, by 2024. The proceeds are expected to be used for the acquisition of shopping centers and office buildings from Central Pattana Group. The LTV ratio of CPNREIT would then stay at 35% and the debt to EBITDA ratio should remain at the level of 5 times or below by 2023.

We view the renewal obligation of Central Rama 2, worth THB20.1 billion, to be temporary during the pre-lease period from 2020 to 2025. We expect this obligation will ultimately be financed by 70% equity and 30% debt in 2025 once the new lease term is executed.

The financial covenants on CPNREIT's bonds and bank loans require the trust's LTV ratio (excluding lease liability in loans) to remain below 60% and the debt service coverage ratio (DSCR) to stay above 1.2 times. As of June 2022, the trust's LTV ratio (excluding lease liability in loans) was 28% and DSCR was 1.57 times. The trust should have no problem keeping the LTV ratio and DSCR in compliance with the debenture and bank loan covenants.

Adequate liquidity

We expect the trust's liquidity to be adequate for the next few years. As of June 2022, CPNREIT's sources of liquidity included cash on hand of THB1.5 billion and investments in securities of THB1.2 billion at fair value. The trust also had undrawn committed credit facilities from banks worth THB1.2 billion. Funds from operations (FFO) in 2022 are forecast at THB3.3 billion.

Debts due in the second half of 2022 total THB70 million. Maturing debts in 2023 comprise long-term debt of THB2.7 billion and debentures of THB1.8 billion. The trust plans to refinance the maturing debentures with new debentures issuances. Bank loans will be either repaid or refinanced by back-up facilities.

CPNREIT's liquidity uses also include dividend payments of at least 90% of adjusted net investment income and operating expenses at the REIT level, expected to be THB1.0-1.5 billion annually during 2022-2024.

As of June 2022, the trust had THB22.6 billion of debt (per priority debt consideration), including THB17.3 billion in senior unsecured debentures and THB5.3 billion in unsecured bank loans. All debts were unsecured debts with pari passu ranking.

BASE-CASE ASSUMPTIONS

- CPNREIT to provide rental fee discounts for shopping centers of 15% from the 2019 level in 2022 and 5% in 2023. Rental fees in 2024 will revert to near the 2019 level.
- Rental and service income of the trust in 2022 to be the same as the 2019 level. Rental and service income will improve to THB6.3-THB7.5 billion per annum during 2023-2024.
- New asset acquisitions worth 16.5 billion to be executed in 2023 and 2024.

RATING OUTLOOK

The “negative” outlook reflects an uncertainty of asset acquisitions and equity injections, leading to weaker financial performance and higher financial leverage than expected.

RATING SENSITIVITIES

CPNREIT’s ratings could be revised downward should the trust’s operating performance and/or financial profile experience a deeper deterioration than expected. On the contrary, CPNREIT’s outlook could be revised back to “stable” if the trust’s financial leverage improves with the LTV ratio staying below 35% and/or the debt to EBITDA ratio staying below 5 times on a sustained basis.

COMPANY OVERVIEW

CPNREIT was founded as part of the process to convert CPN Retail Growth Leasehold Property Fund (CPNRF), a property fund, into a real estate investment trust or “REIT”. CPNRF was established and listed on the Stock Exchange of Thailand (SET) in 2005. Upon the conversion in December 2017, CPNREIT acquired CPNRF’s entire property portfolio, including Central Rama 2, Central Rama 3, Central Pinklao, Central Chiangmai Airport, and two office buildings of Central Pinklao. At the same time, CPNREIT invested in Central Pattaya and Hilton Pattaya. The trust acquired two office buildings, The 9th Towers and Unilever House, from GLANDRT in March 2020 and invested in Central Marina and Central Lampang in February 2021. As of June 2022, CPN was the trust’s largest unitholder with a 30.28% stake.

The property portfolio of the trust currently comprises seven shopping centers, with net leasable area (NLA) of 250,562 sq.m., four office buildings, with NLA of 111,657 sq.m., and one hotel, with 304 rooms. The assets are located in Bangkok, Chiangmai, Chonburi, and Lampang provinces. CPN REIT Management Co., Ltd., a wholly owned subsidiary of CPN, acts as the REIT manager. CPN is the property manager of assets acquired from itself. Grand Canal Land PLC (GLAND) is the property manager of The 9th Towers, and Sterling Equity Co., Ltd., a wholly-owned subsidiary of GLAND, is the property manager of Unilever House. The trust subleases the hotel to CPN Pattaya Hotel Co., Ltd., a subsidiary of CPN, as a special purpose vehicle (SPV). Hilton Hotels and Resorts acts as the hotel manager.

KEY OPERATING PERFORMANCE
Table 1: CPNREIT's Property Portfolio

	Central Rama 2	Central Rama 3	Central Pinklao	Central Chiangmai Airport	Central Pattaya	Central Marina	Central Lampang
Type	Shopping center	Shopping center	Shopping center	Shopping center	Shopping center	Shopping center	Shopping center
Location	Bangkok	Bangkok	Bangkok	Chiangmai	Chonburi	Chonburi	Lampang
Net leasable area (sq.m.)	88,802	36,045	27,712	37,083	29,388	15,453	16,080
OR (%) (as of 30 Jun 2022)	92	94	98	96	91	90	93
Investment at fair value (Mil. THB) (as of 30 Jun 2022)	26,458	12,753	3,204 (incl. office buildings)	10,435	7,279	2,188	2,934
Remaining leasehold period (years)	3+30	13+30+30	3	22	15	13	20

	Office Tower A at Pinklao	Office Tower B at Pinklao	The 9 th Towers	Unilever House	Hilton Pattaya
Type	Office	Office	Office	Office	Hotel
Location	Bangkok	Bangkok	Bangkok	Bangkok	Chonburi
Net leasable area (sq.m.)	22,762	11,334	59,034	18,527	304 rooms
OR (%) (as of 30 Jun 2022)	77	80	84	100	79
Investment at fair value (Mil. THB) (as of 30 Jun 2022)			5,860	1,356	3,668
Remaining leasehold period (years)	3	3	25	13	15

Source: CPNREIT

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS*
Unit: Mil. THB

	Jan-Jun 2022	-----Year Ended 31 December -----			
		2021	2020	2019	2018
Total operating revenues	2,309	3,524	4,062	5,131	4,923
Earnings before interest, taxes, depreciation, and amortization (EBITDA)	1,799	2,453	3,012	4,208	3,984
Funds from operations (FFO)	1,506	1,854	2,420	3,704	3,581
Adjusted interest expense	293	599	592	505	403
Investments in leasehold properties at fair value	76,135	75,371	68,270	44,472	44,750
Total assets	80,101	78,971	71,577	46,687	46,850
Adjusted net debt (excluding lease liability)	20,328	20,688	21,068	13,367	13,441
Lease liability	20,158	19,315	17,727	-	-
Adjusted equity	33,977	33,819	28,044	29,701	29,995
Adjusted Ratios					
EBITDA margin (%)	77.91	69.60	74.14	82.02	80.92
Pretax return on permanent capital (%)	5.30 **	4.56	6.32	9.47	9.00
EBITDA interest coverage (times)	6.13	4.09	5.09	8.34	9.88
Debt to EBITDA (times)	6.77 **	8.43	6.99	3.18	3.37
FFO to debt (%)	11.91 **	8.96	11.49	27.71	26.64
Debt to capitalization (%)	37.43	37.95	42.90	31.04	30.94
Loan to fair value of total assets (%) (according to bond covenants)	28.21	28.57	32.18	31.11	30.95
Loan to fair value of total assets (%) (excluding lease liability from loan and total assets)	37.70	37.82	42.78	31.11	30.95

* Consolidated financial statements

** Annualized with trailing 12 months

RELATED CRITERIA

- Corporate Rating Methodology , 15 July 2022
- Key Financial Ratio and Adjustments for Corporate Issuers, 11 January 2022
- Rating Methodology for Real Estate for Rent Companies, 15 July 2021
- Issue Rating Criteria, 15 June 2021

CPN Retail Growth Leasehold REIT (CPNREIT)

Company Rating:	AA
Issue Ratings:	
CPNREIT232A: THB1,795 million senior unsecured debentures due 2023	AA
CPNREIT243A: THB2,000 million senior unsecured debentures due 2024	AA
CPNREIT263A: THB1,500 million senior unsecured debentures due 2026	AA
CPNREIT268A: THB1,650 million senior unsecured debentures due 2026	AA
CPNREIT272A: THB2,000 million senior unsecured debentures due 2027	AA
CPNREIT288A: THB7,390 million senior unsecured debentures due 2028	AA
CPNREIT318A: THB1,000 million senior unsecured debentures due 2031	AA
Rating Outlook:	Negative

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