

Thailand Prime Property Freehold and Leasehold Real Estate Investment Trust

No. 150/2019

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CORPORATES

Company Rating: A-
Outlook: Stable

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RATIONALE

TRIS Rating assigns the company rating on Thailand Prime Property Freehold and Leasehold Real Estate Investment Trust (TPRIME or “trust”) at “A-” with a “stable” outlook. The rating reflects the trust’s quality assets in prime locations of Bangkok, reliable source of cash flow from contract-based rental income, and low financial leverage. However, the rating is partially offset by portfolio concentration in only two assets and its exposure to contract renewal risk.

KEY RATING CONSIDERATIONS

Good quality assets in prime locations

TPRIME’s assets comprise two office buildings, “Exchange Tower” (EXCHANGE) and “Mercury Tower” (MERCURY). The total leasable area of both buildings is 67,000 square metres (sq.m.). TPRIME holds 99% of Exchange Tower Ltd., the company that owns EXCHANGE. In addition, TPRIME is entitled to a 19-year lease contract (2016-2035) in MERCURY.

Both buildings are grade A office buildings located in the central business district (CBD) with direct access to BTS Skytrain stations. EXCHANGE was built in 2004 and MERCURY was built in 2001. Both buildings are well maintained and receive favorable rental rates. The average rent was around Bt1,000 per sq.m. per month for EXCHANGE and around Bt950 per sq.m. per month for MERCURY in 2018, compared with the industry-wide rental rate of around Bt926 per sq.m. per month for grade A office buildings.

Stable cash flow

TRIS Rating expects both EXCHANGE and MERCURY to generate stable income over the next two years. Both EXCHANGE and MERCURY were well-occupied with occupancy rate (OR) of more than 90% and 89%, respectively, during 2016-2017. ORs improved to 98%-99% for EXCHANGE and to 95%-96% for MERCURY during 2018 through the first six months of 2019, compared with the industry average OR of around 93% in 2018. EXCHANGE’s rental rate grew 5% per annum on average during 2016-2018 while MERCURY’s rental rate grew about 2% per annum over the same period.

TRIS Rating expects TPRIME’s revenue to steadily increase. Given the good quality of its assets and the favorable leasing conditions in the office space market in Bangkok, the trust should be able to maintain the ORs above 90% and achieve rental rate growth of 2% per annum during 2019-2021 for both buildings. Under TRIS Rating’s base case, TPRIME’s earnings before interest, tax, depreciation and amortization (EBITDA) should maintain at around Bt500-Bt600 million per annum and funds from operations (FFO) at around Bt400 million per annum during 2019-2021.

Asset concentration risk

TRIS Rating holds the view that TPRIME’s assets are highly concentrated in terms of the number of properties and tenants. EXCHANGE contributed around 63% of total rental and service income and MERCURY made up the rest. The trust’s performance relies heavily on both assets. However, both buildings have insurance policies, including industrial all-risk insurance and business interruption insurance to help mitigate risk.

In addition, TPRIME is exposed to some degree of tenant concentration risk. The top-ten tenants occupied 47% of total leasable area for EXCHANGE and 54% of total leasable area for MERCURY in 2018. However, there is no single tenant with more than 5% of total leasable area of the trust.

Exposure to contract renewal risk

In TRIS Rating's view, TPRIME is exposed to some contract renewal risk. Most of TPRIME's lease contracts have a three-year lease term. Around 23% of total leasable space will expire in 2019, 25% in 2020, 46% in 2021, and 6% in 2022. Lease contract expirations are quite concentrated in 2021, since lease contracts of 10 major lessees of both buildings will expire in the same year. However, TPRIME's management believes that most lessees will renew their contracts since the cost of moving offices is quite high and some anchor tenants recently invested in office renovations.

Generally, the asset manager will negotiate the lease renewal with tenants about six months in advance of expiration. Thus, the trust has time to look for new tenants should the lessees decide not to renew their contracts. According to the trust's record, it was able to find new tenants to replace one of its major tenants, TRUE Fitness, within six months. TRUE Fitness ended its lease contracts without advanced notice to the trust. TRUE Fitness rented 4,639 sq.m. of retail space at EXCHANGE, accounting for 11% of total leasable area of EXCHANGE and 7% of total leasable area of the trust. The trust was able to find three new tenants to fill the vacant space and also achieved better rental rates.

Low financial leverage

TRIS Rating expects TPRIME to maintain its conservative financial policy. TPRIME's debt to capitalization ratio has stood at 20%-21% during 2018 through the first six months of 2019. The debt to EBITDA ratio was 2.8 times in 2018 and 2.6 times in the first six months of 2019. Under TRIS Rating's base case, TPRIME's debt to capitalization ratio should stay below 30% during 2019-2021 despite its plan to acquire new assets. TPRIME's net debt to EBITDA ratio should also stay below 3 times.

Regarding the financial covenants of TPRIME's bank debt, the trust has to maintain the loan to fair value of the total asset ratio below 35% and the interest-bearing debt to EBITDA less than 6 times. At the end of June 2019, TPRIME's loan to fair value of the total asset ratio was 23% and interest-bearing debt to EBITDA was 3.4 times. We believe the trust should have no problem complying with its financial covenants.

Adequate liquidity

TRIS Rating views the trust's liquidity profile as adequate. The trust's sources of liquidity include cash on hand of around Bt500 million and available facilities from financial institutions of Bt110 million. The FFO to total debt ratio was around 20% and the EBITDA interest coverage ratio was 6-7 times in 2017-2018. TRIS Rating expects TPRIME's FFO will hover around Bt400 million per annum during 2019-2021 and the FFO to total debt ratio to stay in the mid-20% range. The trust has no debt due in 2019-2020, but its bank loans of Bt2 billion will become due in 2021. TRIS Rating expects that the trust should be able to refinance its debt given the trust's quality assets and stable cash flow.

BASE-CASE ASSUMPTIONS

- Under TRIS Rating's base-case scenario, rental rates of both buildings will grow at 2% per annum during 2019-2021.
- EXCHANGE's OR will range between 95%-98% and MERCURY's OR will range between 92%-95% during 2019-2021.
- TPRIME's EBITDA margin will be maintained at around 59% during 2019-2021.
- Capital expenditure will be around Bt30 million per annum during 2019-2021.

RATING OUTLOOK

The "stable" outlook reflects the expectation of TRIS Rating that TPRIME's assets will generate stable cash flow. Under TRIS Rating's base case, TPRIME's debt to total capitalization ratio should stay below 30% and its debt to EBITDA ratio should not be higher than 3.5 times on a sustained basis.

RATING SENSITIVITIES

We could lower the rating should TPRIME engage in large, debt-funded acquisitions such that the debt to capitalization ratio exceeds 30% and/or the debt to EBITDA ratio rises above 4 times. We could also lower the rating if TPRIME's operating performance deteriorates significantly, perhaps from stress in the office space for rent market. On the other hand, we would consider an upgrade for the rating if the trust materially increases its scale and diversifies its asset base while maintaining its financial profile at the current level.

COMPANY OVERVIEW

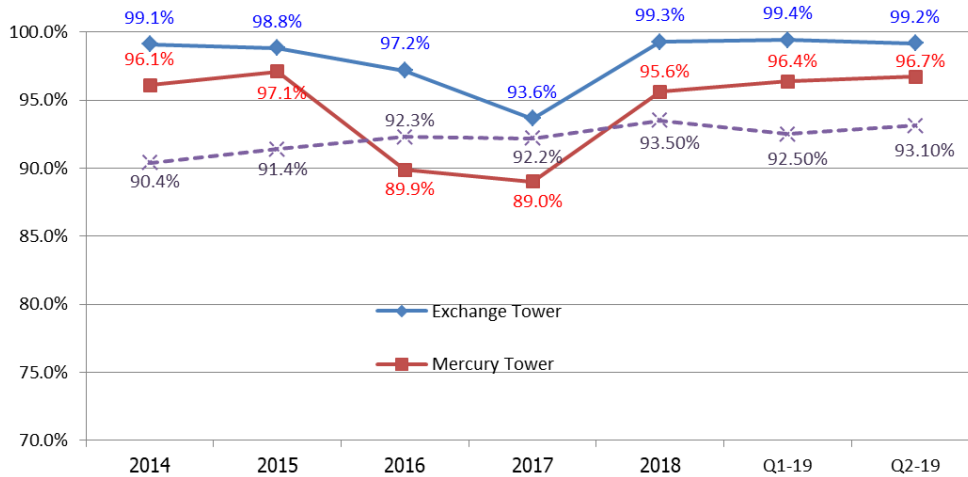
TPRIME is a non-redeemable and indefinite real estate investment trust (REIT). The trust was established in October 2016 with the initial objective to invest in leasehold right of MERCURY and in the 99% shares of Exchange Tower Ltd., which owns EXCHANGE. The trust is a non-sponsored REIT with diverse major unit holders including insurance companies, funds, and other financial institutions. The REIT manager is SCCP REIT Co., Ltd. (SCCP). SCCP is equipped with highly experienced board members and management teams. Property managers are CBM Facilities Management (Thailand) for EXCHANGE and Jones Lang LaSalle Management for MERCURY.

The trust’s assets comprise two office buildings, EXCHANGE and MERCURY, with a total net leasable area of around 67,000 sq.m. Office space accounts for 79% of the total leasable area while retail space makes up the rest. Both buildings are located in prime areas. EXCHANGE is located on the corner of Asoke junction and connected to Asoke BTS station via a sky bridge. MERCURY sits on the corner of Ploenchit road and Langsuan street with a direct walkway link to Chidlom BTS station. As of June 2019, the fair value of TPRIME’s assets was Bt8.09 billion.

The trust’s rental and service income was Bt829 million in 2017 and Bt927 million in 2018. EXCHANGE generated about 60% of rental and service income and the rest came from MERCURY. The top-ten tenants for each building occupied 45%-54% of total net leasable space during 2017-2018.

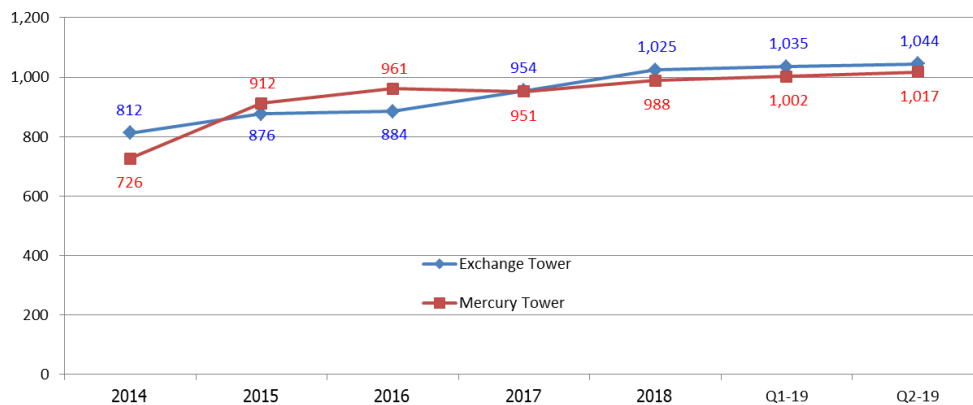
KEY OPERATING PERFORMANCE

Chart 1: Occupancy Rate and Industry Average of Office for Rent

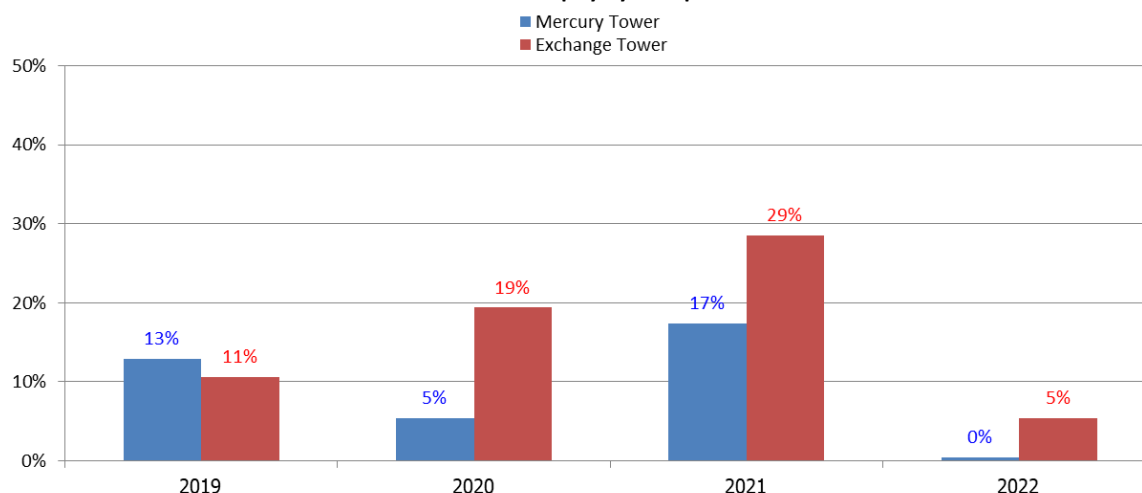


Sources: TPRIME and CB Richard Ellis (CBRE)

Chart 2: Rental Rate for Overall Tenants



Source: TPRIME

Chart 3: Lease Expiry by Occupied Area


Source: TPRIME

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS

Unit: Bt million

	Jan-Jun 2019	---Year Ended 31 December---		
		2018	2017	2016 *
Total operating revenues	487	930	829	162
Operating income	325	578	476	103
Earnings before interest and taxes (EBIT)	303	533	432	95
Earnings before interest, taxes, depreciation, and amortization (EBITDA)	327	580	478	105
Funds from operations (FFO)	246	428	347	75
Adjusted interest expense	44	88	89	21
Capital expenditures	0	0	0	0
Total assets	8,891	8,721	8,357	8,106
Adjusted debt	1,599	1,604	1,685	1,623
Adjusted equity	6,369	6,160	5,856	5,540
Adjusted Ratios				
Operating income as % of total operating revenues (%)	66.88	62.12	57.37	63.69
Pretax return on permanent capital (%)	6.86 **	6.52	5.49	1.23 ***
EBITDA interest coverage (times)	7.49	6.59	5.40	5.07
Debt to EBITDA (times)	2.60 **	2.77	3.53	15.45 ***
FFO to debt (%)	28.38 **	26.66	20.58	4.62 ***
Debt to capitalization (%)	20.07	20.66	22.34	22.66

* For the period from 11 Oct 2016 to 31 Dec 2016

** Annualized with trailing 12 months

*** Non-annualized

RELATED CRITERIA

- Rating Methodology – Corporate, 26 July 2019
- Key Financial Ratios and Adjustments, 5 September 2018
- Real Estate Investment Trust, 12 October 2016

Thailand Prime Property Freehold and Leasehold Real Estate Investment Trust PLC (TPRIME)

Company Rating:	A-
Rating Outlook:	Stable

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