

CHARN ISSARA DEVELOPMENT PLC

No. 98/2023
31 May 2023

CORPORATES

Company Rating: BB
Outlook: Stable

Last Review Date: 30/05/22

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 tight but manageable liquidity. The rating also takes into consideration our concerns over the reimposition of the loan-to-value (LTV) rules and interest rate hikes which could negatively impact housing demands in the short to medium term.

KEY RATING CONSIDERATIONS

Rating constrained by modest and volatile revenue and earnings

CI’s revenue and earnings are small and volatile. Its residential portfolio is highly concentrated in very few projects while its hotel portfolio is also small and was hit hard by the COVID-19 pandemic. CI’s revenues and earnings before interest, taxes, depreciation, and amortization (EBITDA) have ranged from around THB1.3-THB2.0 billion and THB100-THB350 million, respectively, over the last three years. In 2022, real estate sales were the company’s primary source of revenue, contributing 56% of total operating revenue, while the revenue contributions from hotel operations and other rental and services were 32% and 3%, respectively.

At the end of March 2023, the company had 12 active residential property projects, located mainly in Bangkok and popular tourist destinations. The value of unsold units (both built and un-built) totaled THB6.4 billion. CI’s backlog stood at THB2.4 billion, which is expected to be recognized as revenues in 2023-2024. Nearly 80% of the backlog came from two condominium projects, The Issara Sathorn and Sasara.

CI’s hotel portfolio comprises Sri Panwa Hotel which includes Yaya, Baba Beach Club Hua Hin which includes Habita Seaview, and Baba Beach Club Natai. Revenue and EBITDA from hotels in 2022 were THB672 million and THB73 million, improving from THB337 million and negative THB11 million, respectively.

Acceptable brand recognition in the middle- to high-end segments

We consider CI’s market presence in the residential property and hotel businesses to be reputable in terms of the quality of products and services offered as well as its unique style. Its residential products and hotels mainly target middle and high-end customers. CI offers landed property products with unit prices ranging from THB10-THB100 million for single detached houses (SDH) and THB30-THB60 million for residential villas. Condominium units are priced from THB60,000 to THB200,000 per square meters (sq.m.)

CI usually develops residential projects and hotels in the same areas, mainly in major tourist destinations like Phuket, Phangnga, and Hua Hin. CI currently operates hotels with a total of 240 keys. The average room rate (ARR) is in the range of THB30,000 to THB50,000 per room per night for villas and THB5,000 to THB15,000 per room per night for typical hotel rooms. We view that the development of mixed-use products would enhance the property value of CI’s residential units.

Recovery in performance anticipated

Following the easing of the pandemic situation in 2022, there have been signs of reviving numbers of foreign homebuyers and tourist arrivals in Thailand.

This should help improve the operating performance of CI's hotel and real estate businesses. We expect CI's total operating revenue to range from around THB2.2-THB2.4 billion per annum in 2023-2025, except for 2024 when its revenue could peak at THB3.9 billion boosted by transfers of The Issara Sathorn and Sasara projects which are due to be completed in late 2023. The average gross profit margin should remain above 25% while EBITDA margin from normal operations should be at least 14%.

In our base-case forecast, we project revenue from real estate sales of THB1.0-THB1.3 billion in 2023 and 2025, with revenue from residential sales climbing to THB2.8 billion in 2024. The gross profit margin from the real estate business is expected to remain at 30%-31%. We project a recovery of occupancy rates (OR) and average room rates for all hotels in 2023-2025. Thus, revenue from hotel operations should gradually revive to THB850-THB900 million per annum in that period, up from THB672 million in 2022 and THB337 million in 2021. The gross profit margin from hotel operations is expected to improve to 10%-15% in 2023-2025, from 8% in 2022 and the negative territory in 2019-2021.

Reimposition of LTV rules and interest rate hikes may have negative impacts

The reimposition of LTV rules and rising interest rates could dampen housing demand in the short to medium term. From January 2023, banks have been obliged to cap LTV at 80%-90% for second mortgage contracts and at 70% for third mortgage contracts. In our view, the LTV rules will generally have greater impacts on the middle and high-end housing segments since these buyers may have more than one mortgage contract. However, the LTV limits should have no impact on CI's target customers in the luxury housing segment as they tend to be cash buyers.

On the other hand, rising interest rates are likely to have a significant impact on the debt servicing capacity of homebuyers, especially those in the lower-income segment. Interest rate hikes will also affect the funding costs of developers. However, given the easing pressure from both foreign exchange and inflation, we do not expect the Bank of Thailand (BOT) to raise the policy rate by more than two or three times this year. The BOT has already raised the policy rate twice this year, by 25 bps in January and by another 25 bps in March.

High financial leverage

We expect CI's financial leverage to remain high over the next few years. We project the debt to capitalization ratio to rise to 75% in 2023, before falling to 68%-70% in 2024-2025 with the transfer of two condominium projects and the asset sales to the Sri Panwa Hospitality Real Estate Investment Trust (SRIPANWA). The financial covenants on CI's bank loans and debentures require the company's interest-bearing debt to equity ratio to remain below 3.75 times. At the end of March 2023, the ratio was 1.97 times. We expect the company to prudently manage its capital structure to comply with the financial covenants. CI's funds from operations (FFO) to debt ratio is expected to remain in negative territory this year before recovering to around 6%-8% in 2024-2025. Its debt to EBITDA ratio is expected to decline from more than 20 times this year to below 10 times in 2024-2025.

Our base-case scenario assumes CI will launch new condominium projects worth THB1.7 billion in 2023 and two landed property projects worth THB6.4 billion in 2024. The budget for land acquisition will be THB850 million in 2023, THB500 million in 2024, and THB100 million in 2025. Our base-case assumption also incorporates sales of Habita Seaview Hua Hin and Sripanwa Yaya to SRIPANWA with lease back in 2024 and 2025, respectively. Proceeds from the asset sales are expected to be around THB2.0-THB2.4 billion in total, with an expected gain on sales of around 20%-30%. In our view, CI's strategy to sell its assets to SRIPANWA will help improve its earnings and capital base. However, any delay in its sales could erode CI's equity and drag down its financial position which could trigger a downward revision of the rating and/or outlook.

Tight but manageable liquidity

We expect CI's liquidity to be tight but manageable over the next 12 months. As of March 2023, the company had maturing debts over the next 12 months totaling THB3.6 billion, comprising THB1.2 billion in debentures, THB1.2 billion in long-term loans, THB0.6 billion in short-term loans, and THB0.6 billion in lease liability. CI's sources of liquidity included cash on hand of THB995 million, investments in marketable securities of THB515 million, and unused committed credit facilities of THB1 billion. Also, CI had unencumbered land banks at book value of THB742 million, which could be pledged as collateral for new loans (if needed). CI usually refinances its matured debentures with new debenture issuances. CI issued THB700 million of senior unsecured debentures in late March 2023 to refinance the THB290 million in senior unsecured bonds coming due in April 2023. Project loans are normally repaid with the proceeds from the underlying projects' unit transfers.

At the end of March 2023, CI had total debt of THB5.6 billion (per priority debt consideration). The company's priority debt, including secured debts at the parent company and total debts of its subsidiaries, was THB4.1 billion. These translate to a priority debt to total debt ratio of 73%. Thus, in our view, CI'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 for CI's operations in TRIS Rating's base-case forecast for 2023-2025:

- CI to launch new condominium project worth THB1.7 billion in 2023 and two landed property projects worth THB6.4 billion in 2024
- Annual budget for land acquisition to be THB850 million in 2023, THB500 million in 2024, and THB100 million in 2025
- Revenue base of THB2.2-THB2.4 billion per annum but reaching THB3.9 billion in 2024 from transfers of the bulk of the condominium backlog
- CI to sell assets to the REIT worth around THB2.0-THB2.4 billion in total in 2024-2025
- EBITDA margin, excluding gain on asset sales to the REIT, of 14% at least

RATING OUTLOOK

The "stable" outlook reflects our expectation that CI's operating performance and financial profile will not further deteriorate from the target levels. We expect CI to keep its debt to capitalization ratio below 75% and its EBITDA margin, excluding gains on asset sales to the REIT, above 14% over the forecast period.

RATING SENSITIVITIES

A downward revision of the rating and/or outlook could occur if CI's operating results and/or financial position significantly deviate from our expectation. Conversely, an upward revision would materialize if CI demonstrates significant and sustainable improvements in its operating and financial performance, such that the FFO to debt ratio improves to a level above 5% and the debt to capitalization ratio stays below 70% on a sustained basis.

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 2023, 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 2023, the residential property portfolio comprised condominiums (47% of the total remaining value of the project portfolio), SDH (30%), and residential villas (22%). CI's existing residential projects are located in Phetchaburi (20% of the total remaining value of the project portfolio), Phuket (21%), Bangkok (52%), Nakorn Ratchasima (3%), and Chiang Mai (5%).

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 invested in a 30% stake of SPWPF. In 2016, SPWPF was converted from a property fund to a REIT named SRIPANWA. Currently, CI directly and indirectly holds 16.8% of SRIPANWA. The company also owns 17.6% of Bangkok Commercial Property Fund (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.

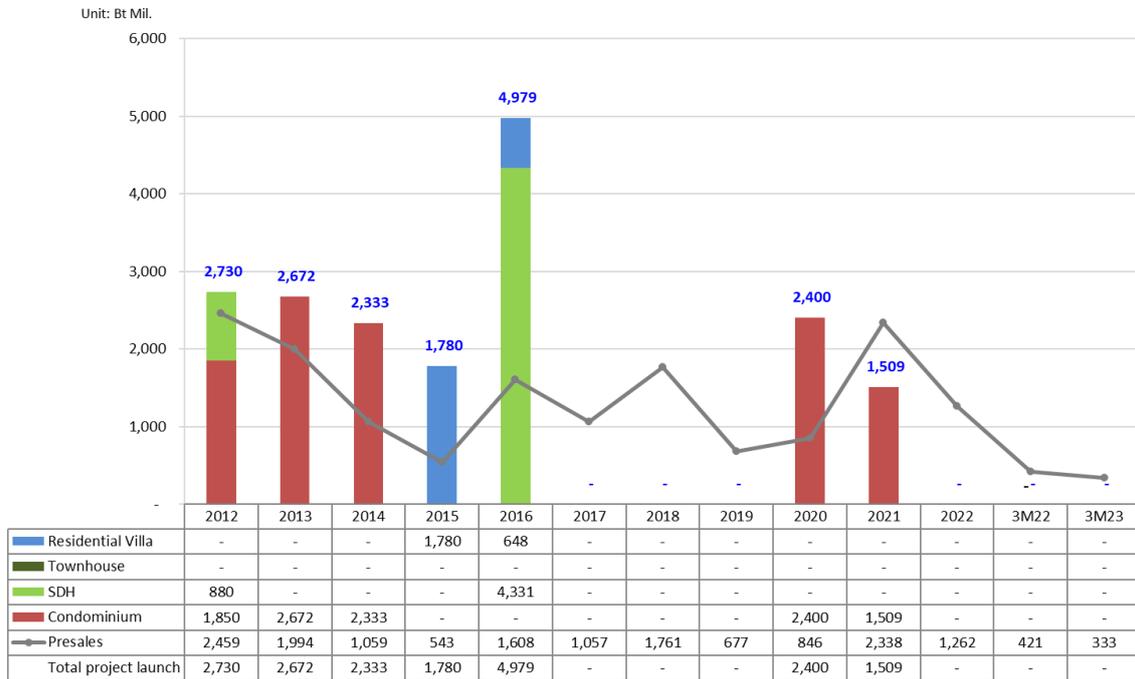
In 2015, CI developed its second mixed-use project in Phangnga under an 86:14 joint venture (JV) with Junfa Real Estate Co., Ltd., a Chinese property developer. The project included 24 villas for sale and a boutique hotel under the brand "Baba Beach".

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.

In July 2022, CI opened Yaya, which is in the same compound as Sri Panwa Hotel. Yaya Sri Panwa includes 24 pool suites and a convention hall.

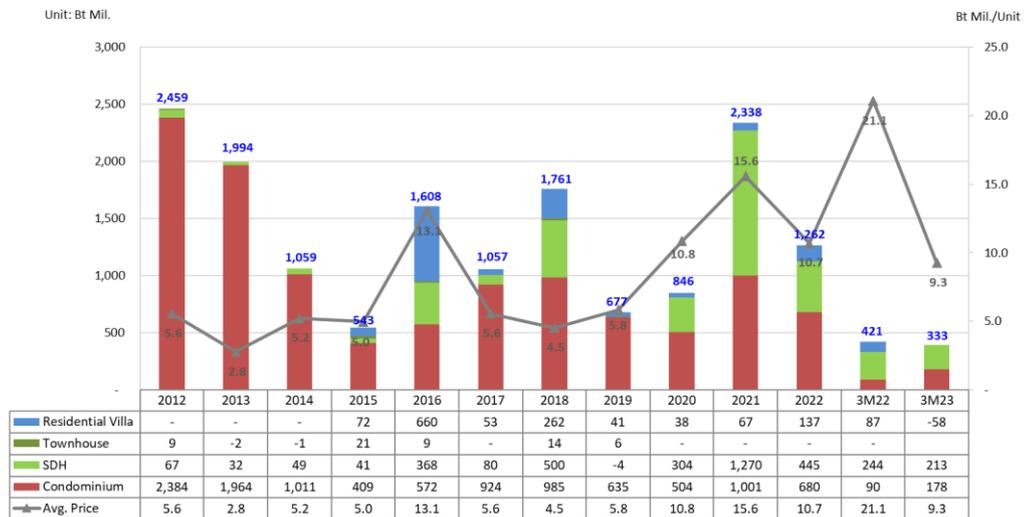
KEY OPERATING PERFORMANCE

Chart 1: Residential Project Launches



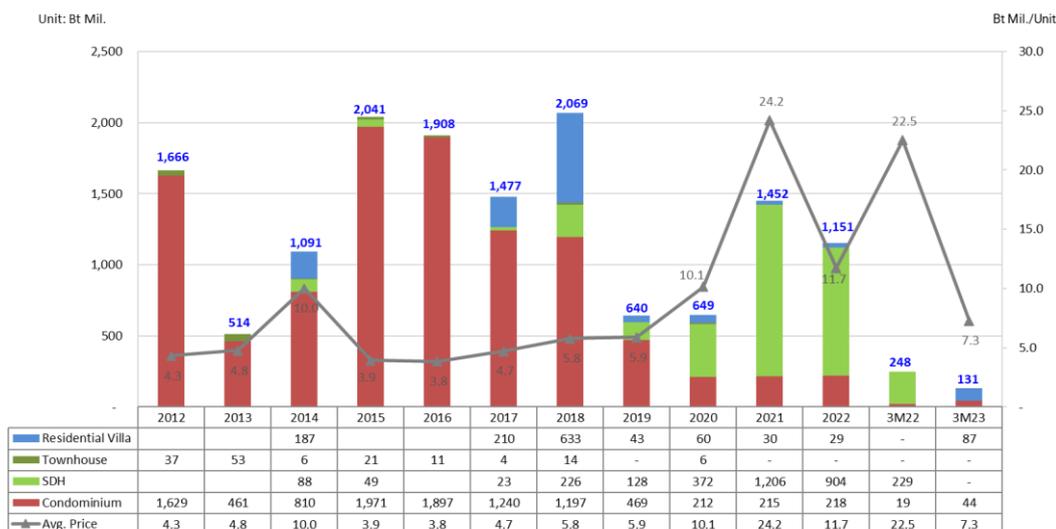
Source: CI

Chart 2: Presales Performance



Source: CI

Chart 3: Transfers Performance



Source: CI

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS*

Unit: Mil. THB

	Jan-Mar 2023	-----Year Ended 31 December -----			
		2022	2021	2020	2019
Total operating revenues	510	2,069	2,001	1,348	1,501
Earnings before interest and taxes (EBIT)	24	15	25	(176)	(276)
Earnings before interest, taxes, depreciation, and amortization (EBITDA)	114	349	299	101	1
Funds from operations (FFO)	(15)	(80)	(149)	(342)	(385)
Adjusted interest expense	129	428	448	443	387
Real estate development investments	4,369	4,226	5,120	5,588	4,939
Total assets	11,699	11,153	10,199	10,805	8,681
Adjusted debt	6,589	6,388	6,296	6,870	5,628
Adjusted equity	2,848	3,021	2,402	2,438	2,949
Adjusted Ratios					
EBITDA margin (%)	22.35	16.85	14.93	7.49	0.09
Pretax return on permanent capital (%)	0.82 **	0.15	0.26	(1.80)	(2.97)
EBITDA interest coverage (times)	0.89	0.81	0.67	0.23	0.00
Debt to EBITDA (times)	15.48 **	18.32	21.07	68.07	4,067.48
FFO to debt (%)	(0.37) **	(1.24)	(2.37)	(4.98)	(6.84)
Debt to capitalization (%)	69.82	67.90	72.38	73.81	65.62

* Consolidated financial statements

** Annualized with trailing 12 months

RELATED CRITERIA

- Homebuilders and Real Estate Developers Rating Methodology, 12 January 2023
- Corporate Rating Methodology, 15 July 2022
- Key Financial Ratios and Adjustments for Corporate Issuers, 11 January 2022

Charn Issara Development PLC (CI)

Company Rating:	BB
Rating Outlook:	Stable

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