

THAILAND PRIME PROPERTY FREEHOLD AND LEASEHOLD REAL ESTATE INVESTMENT TRUST

No. 70/2022
29 April 2022

CORPORATES

Company Rating:	A-
Issue Ratings:	
Senior unsecured	A-
Outlook:	Negative

Last Review Date: 30/04/21

Company Rating History:

Date	Rating	Outlook/Alert
26/09/19	A-	Stable

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RATIONALE

TRIS Rating affirms the company rating on Thailand Prime Property Freehold and Leasehold Real Estate Investment Trust (TPRIME or “trust”) and the ratings on its senior unsecured debentures at “A-”, and revises the rating outlook to “negative” from “stable”. The “negative” outlook reflects TPRIME’s weaker-than-expected operating performance and increasing pressure on the occupancy and rental rates of the trust amid concerns over excess supply of office spaces in the central business district (CBD) and shrinking demand. The ratings are also constrained by portfolio concentration risk in terms of assets, tenants, and lease expiry dates. Nonetheless, the ratings continue to reflect TPRIME’s strong cash flow protection and relatively low financial leverage.

KEY RATING CONSIDERATIONS

Weaker-than-expected operating performance

TPRIME’s operating results fell significantly below our previous forecast. The trust reported a declining trend of average occupancy rate (OR) throughout 2021. The OR of “Exchange Tower” (EXCHANGE) dropped sharply to 78% in the last quarter of 2021 from 94% in the last quarter of 2020. The OR of “Mercury Tower” (MERCURY) decreased to 83% in the fourth quarter of 2021 from 91% in the fourth quarter of 2020. The reported figures fell significantly short of our previous forecast of 85%-90%, and below the industry average of 86% in 2021. The increased vacancy was mainly the result of terminations of contracts and the downsizing of office space by existing tenants.

Lower occupancy in the two office buildings resulted in a 12% year-on-year (y-o-y) decline in TPRIME’s operating revenues in 2021 to THB811 million. The trust’s profitability also softened as its earnings before interest, taxes, depreciation, and amortization (EBITDA) margin declined to 66% in 2021, from 72% in 2020 and 67% in 2019.

Rising pressure on occupancy and rental rates

We view that the trust’s OR and rental rates will likely continue under pressure due to an anticipated influx of office supply in 2022-2023 coupled with shrinking demand for office space. According to CBRE, around 500,000 square meters (sq.m.) and 400,000 sq.m. of new supply are expected to be added to the market in 2022 and 2023, respectively. Meanwhile, the net take-up level of office spaces is predicted to be only 30,000 sq.m.-40,000 sq.m. per annum during the next couple of years. The widening gap between new office supply and take-up demand is being driven by the increasing adoption of remote working and virtual meetings. We assess that the expected slowdown in demand coupled with sizable increases in supply, especially in the CBD, could further depress OR and rental rates over the next three years.

Our base-case forecast projects flat growth in rental rates with OR of both buildings in the 75%-80% range over the next three years. We expect the trust to generate income of THB780 million annually over the forecast period, down from the THB810-THB980 million per annum during the past five years.

Portfolio concentration risk with lower renewal rate

We view TPRIME’s asset portfolio remains highly concentrated in terms of the number of properties, tenants, and lease expiry dates. The trust’s performance relies solely on two assets in two locations, Sukhumvit Road and Ploenchit Road. EXCHANGE contributes around two-thirds of total rental and service

income, and MERCURY makes up the rest. In addition, the top-ten tenants occupied 52% of total occupied area for EXCHANGE and 59% of total leased area for MERCURY. The top-ten tenants of each building contributed 48% of rental and services income for EXCHANGE and 49% for MERCURY. The largest tenant occupied 6% of the trust's total leased area and contributed 5% of its rental and services income.

TPRIME is also exposed to contract renewal risk. Most of TPRIME's lease contracts have a three-year lease term while some retail tenants have a one-year term. As of December 2021, 47% of the existing contracts based on occupied area will expire in 2022, 17% in 2023, and 36% in 2024. Lease contract expirations are highly concentrated in 2022 since the lease agreements of 10 major tenants of both buildings will expire within the same period. Currently, around 70% of the 10 major tenants expired this year already renewed their contracts. However, with softening office space demand accelerated by the pandemic, together with expected excess office supply, we foresee that the renewal rate is likely to continue to drop in the next few years. The renewal rate declined to 75%-77% during 2020-2021 from the pre-pandemic level of 84%-95% during 2017-2019.

Cash-flow protection soften but should remain strong given relatively low debt levels

Despite declines in revenue and profitability, TPRIME's cash-flow protection remains strong due to relatively low financial leverage and lower costs after the implementation of a new property tax law. At the end of December 2021, TPRIME's debt comprised only THB2.05 billion in senior unsecured debentures. TPRIME's debt to capitalization ratio was 20% and the debt to EBITDA ratio was 3 times. The decline in revenue was partly offset by lower costs after the implementation of a new property tax law in 2020. The change in the property tax rate from 12.5% of rental and service income to 0.6%-0.7% of asset value (depending on the asset value) and the government relief measure of 90% reduction in payable tax during the COVID-19 year, substantially lowered the trust's tax expenses. As a result, the EBITDA interest coverage ratio remained high at 8.5 times in 2021.

However, our base case assumptions project TPRIME's earnings to decline slightly due to the expected drop in revenue and the cessation of tax reductions in December 2021. We forecast TPRIME's EBITDA to wane to THB480 million per annum with EBITDA margin at 62% over the forecast period. Its EBITDA interest coverage ratio could decline to around 8-8.5 times over the forecast period. TPRIME's debt to capitalization ratio should stay in the 18%-20% range while its debt to EBITDA ratio is expected to increase slightly to around 3-3.5 times, in absence of new asset acquisitions. Currently, the trust has no concrete plans for new acquisitions. Despite an expected decline in profitability, we do not anticipate that the ratios will deteriorate that much from the current levels as the trust plans to reduce its debt level next year, unless rental and service income turns out to be significantly lower than expected.

The financial covenant on TPRIME's debentures requires the trust to maintain its loan to fair value of total assets (LTV) ratio below 60%. The ratio at the end of December 2021 was 25%. The trust should have no problems remaining in compliance with the debenture covenants.

Manageable liquidity

We assess TPRIME's liquidity to remain manageable over the next 12 months. The trust's sources of liquidity as of December 2021 include cash on hand of THB693 million and available credit lines from financial institutions of THB110 million. We forecast funds from operations (FFO) to stay around THB350 million over the next 12 months. As of December 2021, TPRIME had THB2.05 billion in outstanding debentures, including THB1 billion due in January 2023 and THB1.05 billion due in January 2027. The trust has no debt maturing in 2022.

The trust plans to repay maturing debentures of around THB300-THB500 million and refinance the rest with new debenture issues and/or bank borrowings in 2023. Given its ability to access the capital market, the trust should be able to refinance the maturing debentures as planned. In addition, the trust's high-quality unencumbered assets can be used as collateral for term loans from financial institutions, if needed. The market value of its unencumbered assets at the end of 2021 was THB8.76 billion

BASE-CASE ASSUMPTIONS

Here are our key base-case assumptions for TPRIME's operations during 2022-2024:

- OR for both office buildings in the 75%-80% range
- No growth in rental rates
- EBITDA margin to stay around 62%
- No new asset acquisitions

RATING OUTLOOK

The “negative” outlook reflects our expectation of a deterioration in the trust’s operating performance caused by increasing industry risk from anticipated excess supply of office spaces and shrinking demand. The trust’s occupancy and rental rates will likely continue under pressure over the next three years.

RATING SENSITIVITIES

The ratings on TPRIME could be revised downward should an unfavorable industry environment lead to a deeper-than-expected deterioration in the trust’s operating results and/or financial profile, with the OR drops below 80% and/or the rental rate declines significantly on a sustained basis. In addition, an increase in the debt to EBITDA ratio to a level close to 4 times could also serve as a trigger for a rating downgrade. On the contrary, we could revise the rating outlook on TPRIME to “stable” if its financial profile can be sustained at the current level while its operating performance improves to the extent the OR recovers to around 85%-90% and rental rates stay largely the same as current level.

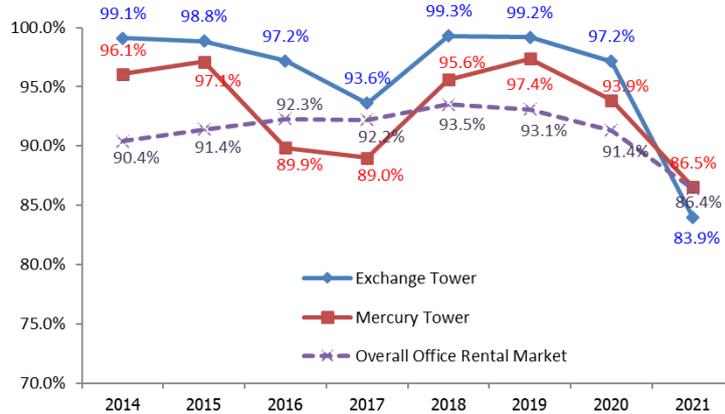
COMPANY OVERVIEW

TPRIME is a non-redeemable and indefinite real estate investment trust (REIT). The trust was established in October 2016 with an initial objective to invest in the leasehold right of MERCURY and in a 99% share of Exchange Tower Ltd., which owns EXCHANGE. The trust is a non-sponsored REIT with diverse major unitholders including insurance companies, funds, and other financial institutions. The REIT manager is SCCP REIT Co., Ltd. (SCCP). SCCP is operated by highly experienced board and management members. Property managers are CBM Facilities & Security 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 67,416 sq.m.. Office space accounts for 79% of the total leasable area while retail space makes up the remainder. Both buildings are located in prime areas. EXCHANGE is located on the corner of Asoke junction and is connected to Asoke BTS station via a sky bridge. MERCURY sits on the corner of Ploenchit Road and Langsuan Road with a direct walkway link to Chidlom BTS station. As of December 2021, the fair value of TPRIME’s assets was THB8.76 billion. The trust’s rental and service income was THB803 million in 2021. EXCHANGE generated about 65% of the rental and service income and the rest came from MERCURY.

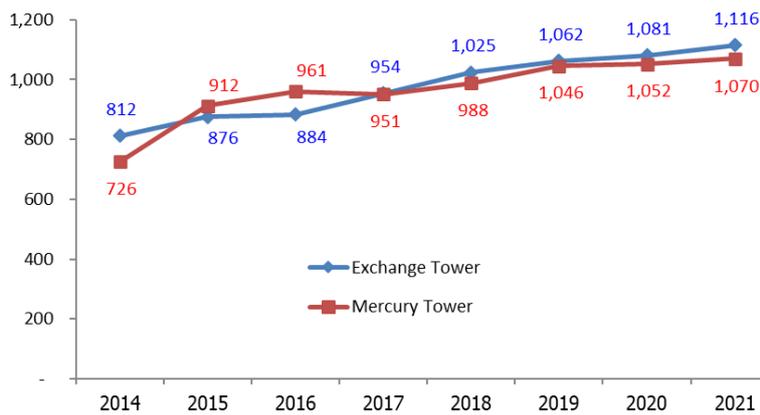
KEY OPERATING PERFORMANCE

Chart 1: Occupancy Rate



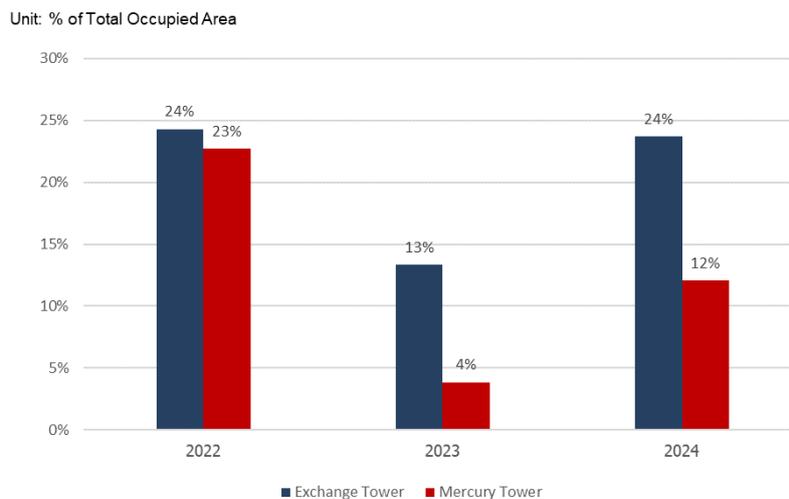
Note: From 2020, OR as average occupancy rate
Sources: TPRIME and CB Richard Ellis (CBRE)

Chart 2: Rental Rate



Source: TPRIME

Chart 3: Lease Expiry



Source: TPRIME

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS*

Unit: Mil. THB

	-----Year Ended 31 December -----				
	2021	2020	2019	2018	2017
Total operating revenues	811	923	979	930	829
Earnings before interest and taxes (EBIT)	499	621	611	533	432
Earnings before interest, taxes, depreciation, and amortization (EBITDA)	532	663	658	580	478
Funds from operations (FFO)	404	519	496	428	347
Adjusted interest expense	62	60	87	88	89
Capital expenditures	0	0	0	0	0
Total assets	9,528	9,478	8,972	8,721	8,357
Adjusted debt	1,673	1,517	1,559	1,604	1,685
Adjusted equity	6,788	6,839	6,420	6,160	5,856
Adjusted Ratios					
EBITDA margin (%)	65.63	71.90	67.24	62.31	57.64
Pretax return on permanent capital (%)	5.48	7.04	7.22	6.52	5.49
EBITDA interest coverage (times)	8.53	10.98	7.53	6.59	5.40
Debt to EBITDA (times)	3.15	2.29	2.37	2.77	3.53
FFO to debt (%)	24.15	34.22	31.78	26.66	20.58
Debt to capitalization (%)	19.78	18.15	19.54	20.66	22.34

* Consolidated financial statements

RELATED CRITERIA

- 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
- Rating Methodology – Corporate, 26 July 2019

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

Company Rating:	A-
Issue Ratings:	
TPRIME231A: THB1,000 million senior unsecured debentures due 2023	A-
TPRIME271A: THB1,050 million senior unsecured debentures due 2027	A-
Rating Outlook:	Negative

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