THAILAND PRIME PROPERTY FREEHOLD AND LEASEHOLD REAL ESTATE INVESTMENT TRUST

No. 46/2020
10 April 2020

CORPORATES

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

Last Review Date: 26/12/19

Company Rating History:

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

Contacts:

Tulyawat Chatkam
tulyawat@trisrating.com

Jutamas Bunyawanichkul
jutamas@trisrating.com

Wajee Pitakpaibulkij
wajee@trisrating.com

Suchada Pantu, Ph. D.
suchada@trisrating.com

WWW.TRISRATING.COM

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-" with a "stable" outlook. The ratings reflect 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 ratings are partially offset by portfolio concentration with only two assets in the portfolio, exposure to contract renewal risk and headwinds from the coronavirus (COVID-19) pandemic.

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 meters (sq. m.). TPRIME has a freehold right in EXCHANGE through a 99% stake of Exchange Tower Ltd., the company that owns EXCHANGE. Besides, 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 while MERCURY was built in 2001. Both buildings are well maintained and command favorable rental rates. The average rent for both buildings was around Bt1,000 per sq. m. per month in 2019, on par with the industry-wide rental rate for grade A office buildings. EXCHANGE's rental rate has grown by 6% per annum over the past 3 years while MERCURY's rental rate has increased by 3% per annum over the same period. Both EXCHANGE and MERCURY are well-occupied with an occupancy rate (OR) of 98%-99% for both buildings in 2019, compared with the industry average OR of around 93% in 2019.

COVID-19 Pandemic to affect the trust's performance in 2020

The COVID-19 outbreak has disrupted the overall economy since late January 2020 and become more severe in March 2020. The outbreak directly affects the trust's retail tenants and indirectly affects office tenants. The government has started to impose various measures to control the spread of the virus such as travel restrictions and mandatory mall and dine-in restaurant closures. Many retail tenants have had to close their stores for as long as the government requires. As for office space, a more diverse tenant mix compared with that of retail space has resulted in a more resilient revenue stream. However, some office tenants' operations may also be severely affected by the pandemic. If the situation is prolonged, some tenants may not be able to make rent payments in-full and on-time. However, TPRIME's office space accounts for 80% of the trust's total lettable area and 70% of total rental and service income, while retail space accounts for the remainder.

TRIS Rating expects the COVID-19 pandemic to put some pressure on the trust's revenue and cash flow in 2020. In our base-case forecast, we expected the trust's overall occupancy to drop by around 15% to the mid-80% range in 2020 as a result of the adverse impacts of the pandemic, based on the assumption that the outbreak can be largely contained by mid-2020. Occupancy is expected to gradually recover to 90%-95% in 2021-2022. TPRIME's earnings before interest, tax, depreciation, and amortization

(EBITDA) are expected to drop to around Bt500 million in 2020 and rebound to Bt550-Bt580 million per annum in 2021-2022.

Asset concentration risk

TRIS Rating holds the view that TPRIME's assets are highly concentrated in terms of the number of properties and tenants. The trust's performance relies solely on these two assets. EXCHANGE contributes around 63% of total rental and service income and MERCURY makes up the rest. However, having insurance policies including industrial all-risk insurance and business interruption insurance for both buildings should in part help mitigate risk.

TPRIME is also exposed to some degree of tenant concentration risk. The top-ten tenants of each building occupied 48% of the total leasable area for EXCHANGE and 54% of the total leasable area for MERCURY in 2019, or around 30% and 20%, respectively, of the total leasable area of the trust. The top-ten tenants of each building contributed 44% of rental and services income for EXCHANGE and 47% for MERCURY. The single largest tenant occupied 5% of TPRIME's total lettable area and contributed around 4.4% of TPRIME's rental and services income.

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 and some retail tenants have a one-year lease term. 24% of total leasable space will expire in 2020, 42% in 2021, and 34% in 2022. Lease contract expirations are quite concentrated in 2021 since the lease contracts of many major lessees will expire in that year. However, TPRIME's management believes that most lessees will renew their contracts because the cost of moving offices is quite high and some anchor tenants recently renovated their offices. The asset manager normally negotiates lease renewals with tenants about six months in advance of expiration. Thus, the trust has time to find new tenants should the lessees decide not to renew their contracts.

However, the COVID-19 pandemic has disrupted the work behavior of several companies. Due to social distancing measures used to prevent the contagion of the disease and advances in technology, the employees of many companies can now easily work from home during the period of travel restrictions. We found that this change in work behavior could pose a threat for office space providers in the medium term as more supply is entering the market in the next few years while demand may not grow at the same rate. However, TPRIME believes that it should be able to maintain its occupancy rate above 90% since both buildings are located in prime areas and rental rates are competitive compared with newly constructed buildings in the CBD.

Low financial leverage

TPRIME's strength is derived from its low financial leverage resulting from the trust's conservative financial policy. The trust's debt to capitalization ratio stood at around 20% in 2018-2019 and the debt to EBITDA ratio improved to 2.4 times in 2019 from 2.8 times in 2018.

Under TRIS Rating's base-case forecast, we incorporate the impact of the COVID-19 pandemic that could cause occupancy to drop to mid-80% territory and gradually recover in subsequent years, based on the assumption that the Coronavirus can be largely contained by around mid-2020. Given the trust's prudent financial policy and resilient revenue stream from office space, TPRIME's debt to capitalization ratio is expected to remain at around 20% during 2020-2022. Its debt to EBITDA ratio is expected to flare to 3.1 times in 2020, settling down to 2.5-2.7 times in 2021-2022.

The trust issued debentures worth Bt2 billion in January 2020 to refinance its bank loan. Bond issuance provides the trust a financial cost saving of around Bt30 million per annum compared with the bank loan. The debentures have a key financial covenant that requires the trust to maintain the loan to fair value of the total asset ratio below 60%. As of December 2019, the ratio was 23%. We believe the trust should have no problem complying with its financial covenants in the next 2-3 years.

Adequate liquidity

TRIS Rating assesses TPRIME's liquidity as adequate. The funds from operations (FFO) to total debt ratio was around 32% and the EBITDA interest coverage ratio was 7.5 times in 2019. TRIS Rating expects TPRIME's FFO to drop to Bt370 million in 2020 and rebound to Bt420-Bt450 million per annum thereafter. The FFO to total debt ratio is forecast to decline to 24% in 2020 and bounce back to around 30% in the following years.

The trust's sources of liquidity include cash and cash equivalents of around Bt650 million and available credit lines from financial institutions of Bt110 million. The trust has no debt due in 2020-2022 but debentures of Bt1 billion will come due in 2023 and another Bt1 billion in 2027. We assess that the trust has some financial flexibility to weather the adverse conditions as its cash on hand is enough to cover more than a year of operating costs. TRIS Rating also expects that the trust should be able to refinance its debt given its quality assets and stable cash flow.

BASE-CASE ASSUMPTIONS

- OR for both buildings to slip to mid-80% in 2020 because of COVID-19, and recover to 90%-95% in 2021-2022.
- Rental rates to stay flat due to pressure from the outbreak and sizable new office space supply in the next 2-3 years.
- TPRIME's EBITDA margin to drop to around 58% in 2020 and stay around 60% in 2021-2022.
- Capital expenditure will be around Bt30 million per annum during 2020-2022.

RATING OUTLOOK

The "stable" outlook reflects the expectation of TRIS Rating that TPRIME's assets will continue to generate stable cash flow. Under TRIS Rating's base case, we expect the trust to be moderately affected by COVID-19 and the outbreak to be largely contained by mid-2020. The debt to EBITDA ratio should rise briefly in 2020, however not beyond 3.5 times. TPRIME's debt to total capitalization ratio should stay below 30%.

RATING SENSITIVITIES

We could lower the ratings if TPRIME's operating performance significantly falls short of our expectation perhaps due to a prolonged COVID-19 outbreak or stress in the office space for rent market or 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. On the other hand, we would consider an upgrade for the ratings if the trust materially increases its scale and diversifies its asset base while maintaining its financial profile at the current level.

COMPANY OVERVIEW

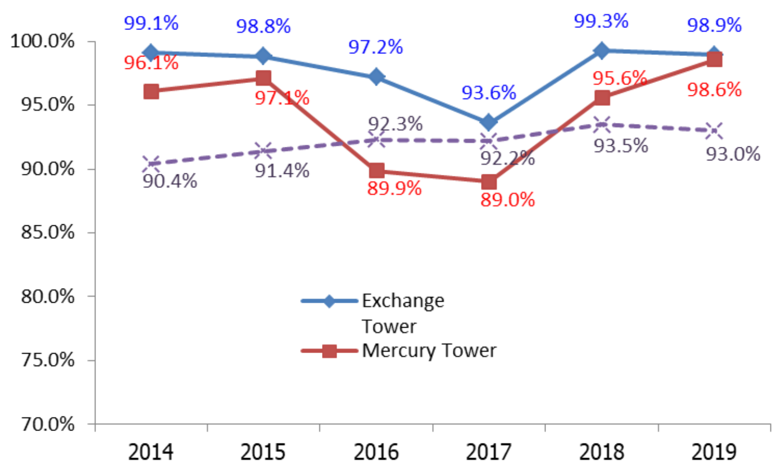
TPRIME is a non-redeemable and indefinite real estate investment trust (REIT). The trust was established in October 2016 with the initial objective to invest in leasehold right of MERCURY and in a 99% share of Exchange Tower Ltd., which owns EXCHANGE. The trust is a non-sponsored REIT with diverse major unitholders including insurance companies, funds, and other financial institutions. The REIT manager is SCCP REIT Co., Ltd. (SCCP). SCCP is equipped with highly experienced board and management members. 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 Road with a direct walkway link to Chidlom BTS station. As of December 2019, the fair value of TPRIME's assets was Bt8.1 billion.

The trust's rental and service income was Bt979 million in 2019. EXCHANGE generated about 63% of rental and service income and the rest came from MERCURY. The top-ten tenants for each building occupied 48%-54% of total net leasable space.

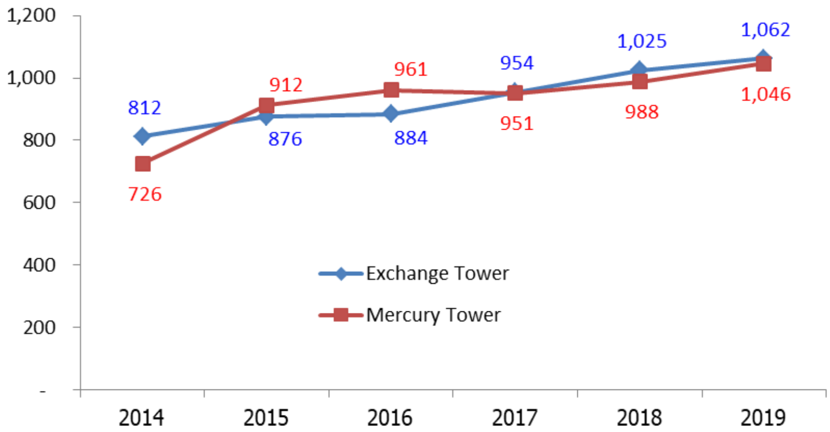
KEY OPERATING PERFORMANCE

Chart 1: Occupancy Rate



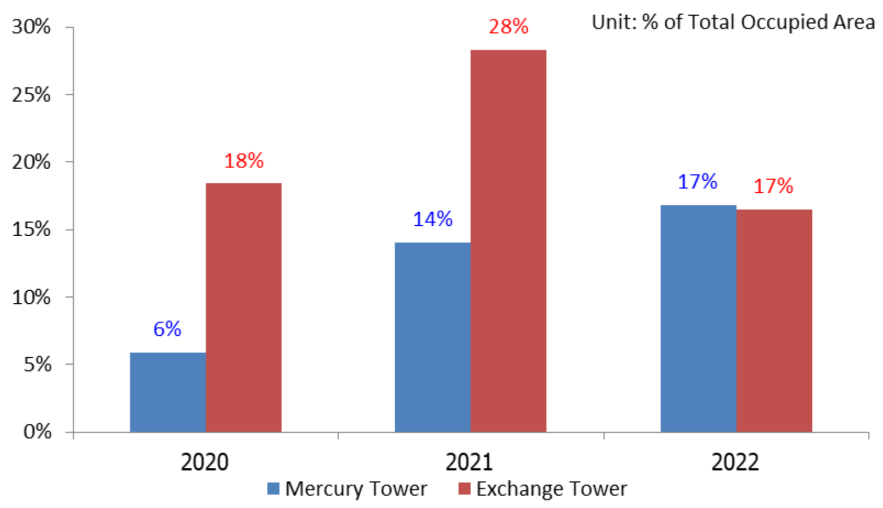
Source: TPRIME

Chart 2: Rental Rate



Source: TPRIME

Chart 3: Lease Expiry



Source: TPRIME

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS

Unit: Bt million

	-----------------Year Ended 31 December -------------				
	2019	**2018**	**2017**	**2016 ***	
Total operating revenues	979	930	829	162	
Earnings before interest and taxes (EBIT)	611	533	432	92	
Earnings before interest, taxes, depreciation, and amortization (EBITDA)	658	580	478	103	
Funds from operations (FFO)	496	428	347	76	
Adjusted interest expense	87	88	89	18	
Capital expenditures	0	0	0	0	
Total assets	8,972	8,721	8,357	8,106	
Adjusted debt	1,553	1,604	1,685	1,623	
Adjusted equity	6,420	6,160	5,856	5,540	
Adjusted Ratios					
EBITDA margin (%)	67.24	62.31	57.64	63.64	
Pretax return on permanent capital (%)	7.22	6.52	5.49	1.19	**
EBITDA interest coverage (times)	7.53	6.59	5.40	5.78	
Debt to EBITDA (times)	2.36	2.77	3.53	15.75	**
FFO to debt (%)	31.91	26.66	20.58	4.67	**
Debt to capitalization (%)	19.48	20.66	22.34	22.66	

* *For the period from 11 Oct-31 Dec 2016*
** *Non-annualized ratios*

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 (TPRIME)

Company Rating:	A-
Issue Ratings:	
TPRIME231A: Bt1,000 million senior unsecured debentures due 2023	A-
TPRIME271A: Bt1,050 million senior unsecured debentures due 2027	A-
Rating Outlook:	Stable

TRIS Rating Co., Ltd.
Silom Complex Building, 24th Floor, 191 Silom Road, Bangkok 10500, Thailand Tel: 0-2098-3000