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# ROYAL ORCHID HOTEL (THAILAND) PLC

No. 33/2021
19 March 2021

## CORPORATES

**Company Rating:** BB-
**Outlook:** Negative

## RATIONALE

TRIS Rating assigns the "BB-" company rating to Royal Orchid Hotel (Thailand) PLC (ROH). At the same time, TRIS Rating assigns a "negative" outlook to the rating. The rating takes into consideration the good location and asset quality of the company's hotel property, which is professionally managed by a world-class hotel chain. The rating is, however, constrained by the expected rise in financial leverage when the planned sale and leaseback transaction of the company's only operating asset to a newly set-up real estate investment trust (REIT) is executed, as the company will incur a financial obligation to buy the asset back from the REIT five years later. The rating also reflects the risk from its reliance on income from a single operating asset, as well as the risk associated with the investment of the sale proceeds.

The "negative" outlook reflects the uncertainty surrounding the recovery prospects of the hotel operation due to the impact of the Coronavirus Disease 2019 (COVID-19) pandemic and our expectation that ROH's credit metrics will continue to be under pressure over the next 12-18 months.

## KEY RATING CONSIDERATIONS

### Planned sales and leaseback transaction

The company is planning to sell the "Royal Orchid Sheraton Hotel & Towers" to a newly established REIT for around THB4.5 billion in the second quarter of 2021. It would lease back the asset for an initial term of three years. The lease could be renewed for another year twice, so the maximum lease term would be five years.

The company has an obligation to buy the asset back from the REIT at the end of the fifth year, at the initial selling price plus some premium. The company also has options to buy the asset back at the end of the third year and the fourth year at pre-determined prices.

The proceeds from the sale would be used for hotel operations during the difficult period due to the impact of the COVID-19 outbreak, and for maintaining and improving the property. The remaining amount would be invested, with the aim of generating a return of no less than 5% per annum. The company plans to fulfil its buyback obligation with the payback from the investment, together with cashflow from its operations. We expect the company to be prudent in investing the proceeds of the asset sale as it would be the main source of funds to fulfill its buyback obligation five years later.

In our analysis, we consider the sale and leaseback transaction akin to borrowing. And we consider the rental payment under the lease terms, together with the buyback premium, to be part of the finance cost. Lastly, we consider the return from investing the sale proceeds to be a part of ROH's earnings before interest, taxes, depreciation and amortization (EBITDA) in each year.

### Hotel performance expected to remain weak in 2021

We project the operating performance of ROH's hotel to remain weak in 2021, before gradually recovering in 2022-2023. Prior to the pandemic, the hotel mainly served foreign travelers, with a focus on Meetings, Incentive Travel, Conventions, and Exhibitions (MICE) and corporate clients. The hotel has been trying to come up with campaigns to attract domestic travelers, but the occupancy rate (OR) has remained low, even before the second outbreak

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began in December 2020. It may take until the end of 2021 before travel restrictions are eased and international travel begins to recover.

Under our base-case scenario, we project ROH's hotel revenue per available room (RevPAR) to be around 80% below the 2019 level in 2021, before improving in 2022 to around 30% below the 2019 level, and in 2023 to around 10% below the 2019 level.

### Reliance on income from a single asset

ROH's hotel property is well maintained and situated in a good location. The company has hired Marriott International Inc. to manage its hotel under the "Sheraton" brand. International hotel chains provide strong brand names, good hotel management systems, and effective sales channels.

However, ROH faces concentration risk as it operates a single property. We consider a well-diversified portfolio of hotels in different locations catering to different market segments to be less susceptible to event risk in general.

### Financial leverage expected to rise significantly after sale and leaseback transaction

After the transaction, the company's net debt will increase to around THB4.5 billion, compared with its debt-free position over the past six years. EBITDA, under our base-case, is projected to be around THB30 million in 2021 and to improve to around THB500 million per annum during 2022-2023. The company's financial leverage, as measured by the adjusted debt to EBITDA ratio, is projected to be over 100 times in 2021, improving to the range of 7-8 times during 2022-2023. ROH's capital budget is projected to be around THB82 million for the next three years.

### No liquidity concern in the near term

ROH's liquidity is adequate. As of December 2020, ROH's sources of funds comprised cash and cash equivalents of THB274 million. The proceeds from the sale of the hotel to the REIT will be in the range of THB4 billion to THB4.5 billion. These sources of cash are sufficient for its uses of funds in the next 12 months, provided that the company reserves enough liquidity before investing the remaining amount.

In 2021, we forecast the company will record a net cash outflow from operations of around THB140 million with budgeted investments of around THB20 million. The company has no debt obligations to repay over the next 12 months.

## BASE-CASE ASSUMPTIONS

- Revenues to be THB170 million in 2021, then increase to around THB700 million in 2022 and THB900 million in 2023.
- EBITDA margin to be around 15% in 2021, then improve to around 60% in 2021 and 2022.
- Total capital spending to be around THB82 million over the three-year forecast period.
- ROH to sell its hotel to the REIT in the second quarter of 2021.

## RATING OUTLOOK

The "negative" outlook reflects the uncertainty of the revival of ROH's operating results following the latest COVID-19 outbreak and the pace and effectiveness of vaccination rollouts. In addition, the recovery of the tourism industry may take longer time than anticipated as the global economic downturn could weaken demand of international travelers.

## RATING SENSITIVITIES

A rating upgrade is unlikely in the near term. However, the outlook could be revised to "stable" if the company's operating performance resumes as normal after the pandemic has been largely contained and cross-border travel restrictions are eased. In contrast, the downside risk scenario would materialize if ROH's financial performance deteriorates more than our projection or if it invests the proceeds from the asset sale in a riskier asset class than expected.

As ROH is a subsidiary of Grande Asset Hotels and Property PLC (GRAND), any downgrade in the credit rating or outlook on GRAND might have an impact on ROH's credit rating or outlook accordingly.

## COMPANY OVERVIEW

ROH was incorporated in 1978 to develop and operate the luxury hotel, "Royal Orchid Sheraton Hotel & Towers". The hotel is located on the Chao Phraya river with 726 rooms. The company has appointed Marriott International Inc. to operate the hotel under the Sheraton brand. As of December 2020, ROH's largest shareholder was GRAND, holding 98% of the total outstanding shares.

## KEY OPERATING PERFORMANCE

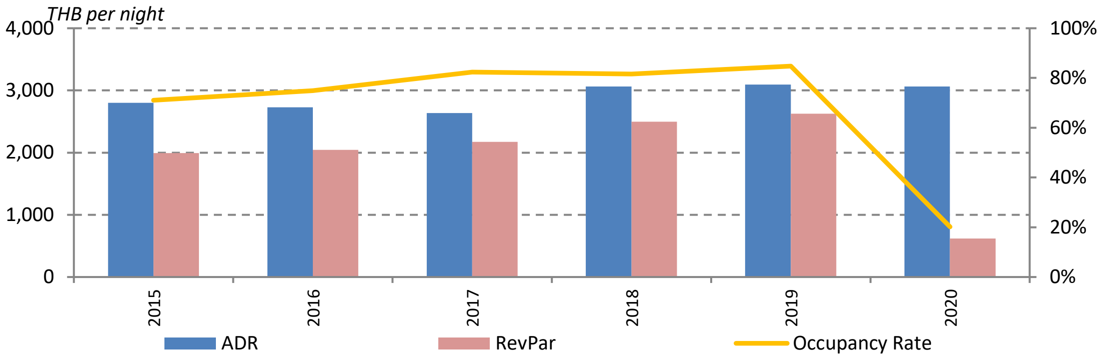
**Table 1: Revenue Breakdown**

*Unit: %*

| Revenue Breakdown | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 |
|---|---|---|---|---|---|---|
| Room | 62 | 63 | 64 | 64 | 65 | 62 |
| Food and beverage | 34 | 33 | 32 | 33 | 32 | 35 |
| Others | 4 | 4 | 4 | 3 | 3 | 3 |
| **Total revenue** | **100** | **100** | **100** | **100** | **100** | **100** |

*Source: ROH*

**Chart 1: ROH's OR, ADR, and RevPar**




*Source: ROH*

## FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS

*Unit: Mil. THB*

| | -----------------------Year Ended 31 December ------------------- | | | | |
|---|---|---|---|---|---|
| | **2020** | **2019** | **2018** | **2017** | **2016** |
| Total operating revenues | 241 | 979 | 937 | 894 | 864 |
| Earnings before interest and taxes (EBIT) | (187) | 184 | 175 | 158 | 133 |
| Earnings before interest, taxes, depreciation, and amortization (EBITDA) | (103) | 262 | 263 | 249 | 226 |
| Funds from operations (FFO) | (71) | 226 | 229 | 218 | 199 |
| Adjusted interest expense | 9 | 2 | 1 | 2 | 2 |
| Capital expenditures | 38 | 23 | 35 | 32 | 44 |
| Total assets | 916 | 1,223 | 1,166 | 1,143 | 1,084 |
| Adjusted debt | 0 | 0 | 0 | 0 | 0 |
| Adjusted equity | 663 | 955 | 940 | 908 | 867 |
| **Adjusted Ratios** | | | | | |
| EBITDA margin (%) | (42.78) | 26.78 | 28.03 | 27.84 | 26.16 |
| Pretax return on permanent capital (%) | (19.97) | 18.08 | 17.87 | 16.76 | 15.38 |
| EBITDA interest coverage (times) | (11.21) | 158.64 | 200.40 | 157.32 | 138.71 |
| Debt to EBITDA (times) | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| FFO to debt (%) | n.m. | n.m. | n.m. | n.m. | n.m. |
| Debt to capitalization (%) | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |

*n.m. not meaningful*

## RELATED CRITERIA

- Group Rating Methodology, 13 January 2021
- Rating Methodology – Corporate, 26 July 2019
- Key Financial Ratios and Adjustments, 5 September 2018

**Royal Orchid Hotel (Thailand) PLC (ROH)**

| | |
|---|---|
| **Company Rating:** | BB- |
| **Rating Outlook:** | Negative |

**TRIS Rating Co., Ltd.**
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