

PROPERTY PERFECT PLC

No. 126/2020
26 August 2020

CORPORATES

Company Rating:	BB
Issue Ratings:	
Hybrid	B
Outlook:	Stable

Last Review Date: 09/08/19

Company Rating History:

Date	Rating	Outlook/Alert
09/08/19	BB+	Negative
20/05/15	BB+	Stable
19/06/14	BB+	Developing
06/12/13	BB+	Stable
18/11/11	BBB-	Negative
18/09/09	BBB-	Stable

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RATIONALE

TRIS Rating downgrades the company rating on Property Perfect PLC (PF) to “BB” from “BB+” and also downgrades the rating on PF’s unsecured subordinated perpetual debentures (hybrid debentures) to “B” from “B+”. The outlook is revised to “stable” from “negative”.

The downgrades reflect PF’s weakening operating performance resulting from the economic fallout from the Coronavirus Disease (COVID-19) pandemic, its high financial leverage, and tight liquidity. The ratings continue to reflect PF’s accepted brand name in the residential property market, its large land bank holdings, and good-quality hotel properties.

The ratings on the hybrid debentures was notched down by three notches from PF’s company rating, due to the debentures’ subordination to PF’s senior debt obligations (two-notch down), and the issuer’s right to defer the coupon payment (one-notch down). The two-notch differential for subordination reflects the risk of potential low rates of principal recovery in a default scenario for hybrid debentures issued by non-investment grade issuers.

KEY RATING CONSIDERATIONS

Weakening performance in the condominium segment

We expect PF’s revenues and profitability to decline further this year. The economic fallout from COVID-19 is suppressing demand for residential properties, especially in the condominium segment. PF’s revenue from residential property development is expected to decrease by 20% year-on-year (y-o-y) in 2020 before gradually increase by 7%-10% annually in the following years. Revenue from condominium projects is expected to shrink to around THB3 billion per annum during 2020-2022 from THB5-THB6 billion per annum during 2016-2019 as demand from both domestic and foreign investors contracts. However, revenue from landed property projects is expected to sustain at around THB8-THB10 billion per annum during 2020-2022.

In our base-case projection, we expect PF to slow down project launches this year due to the drop in demand while the company’s inventory levels remain high. As of June 2020, PF had 56 active landed property projects and 19 existing condominium projects, including owned and under joint ventures (JVs), with total remaining project value of THB55 billion (including built and un-built units). PF had non-moving landed property stock units worth THB1.4 billion and remaining finished condominium units worth THB10 billion. We expect PF to launch more landed property projects, both owned and under JVs, worth THB10 billion per annum but launch fewer condominium projects, worth THB2 billion per annum during 2021-2022. The budget for land acquisition is expected to be around THB1-THB2 billion annually over the next three years.

Hotel business severely affected by the pandemic

We expect the operating performance of PF’s hotels to drop drastically this year, before gradually recovering in 2021-2022. The tourism in Thailand and Japan have been severely affected by the pandemic. Travel restrictions and lockdown measures imposed by authorities in attempts to contain the spread of the virus has severely affected PF’s hotel business starting from the second quarter of 2020. After the outbreak is brought under control domestically in

the second half of 2020, the government has eased its lockdown measures and plans to launch a stimulus package to boost domestic tourism. We view that this should help alleviate the revenue drop-off suffered by the company's hotel properties, especially those in Bangkok and nearby provinces. PF's hotel in Japan, Kiroro, has also been impacted by the local government lockdown measures. The second wave of the virus in Hokkaido has hurt the local tourism sector. TRIS Rating views that the recovery of the tourism industry in both Thailand and Japan remains uncertain. Increasing numbers of infections are still being reported worldwide, which means travel restrictions will likely remain in place for an extended period. Also, the on-going global recession could dampen travel demand even after the pandemic has been largely contained.

In our base-case forecast, we project PF's hotel revenue per available room (RevPar) to fall by around 50% y-o-y on average in 2020, before improving in 2021 to around 30% below the 2019 level and in 2022 to around 5% below the 2019 level. We anticipate revenue from PF's hotels to shrink by around half this year and to gradually recover to THB2 billion in 2021, by which time we expect to see signs of a revival in foreign tourist arrivals. We expect revenue from hotel operation to grow to THB2.7 billion in 2022.

High financial leverage

PF's financial leverage, as measured by the debt to capitalization ratio, was very high at 70% as of June 2020. The net interest-bearing debt to equity ratio at the end of June 2020 was 1.96 times. The key financial covenants on PF's bank loans and debentures require the company to maintain its net interest-bearing debt to equity ratio below 2.5 times. Thus, PF has to carefully manage its net interest-bearing debt to equity ratio in order to comply with the bank loan and bond covenants. PF's funds from operations (FFO) to total debt ratio also turned negative in the first six months of 2020 due to the significant loss from the hotel business. Looking ahead, the slow recovery of the hotel business could drag down PF's bottom line to negative territories during 2020-2021.

PF plans to lower its debt burden by selling some land and hotels. PF has accumulated land bank for residential property projects and leasehold rights for retail and mixed-use projects. Presently, PF owns around 1,300 rai of land, including raw land plots and land under development of its on-going projects. The large pieces of freehold land include a 300-rai plot in Hokkaido, Japan, a 165-rai plot in Chiangmai province, and 100-rai plots on Kanchanapisek road, in the Ramkamhaeng area, and in the Chaengwattana area. PF also holds the leasehold rights to a 21-rai land plot on Ratchadapisek road, a 58-rai plot on Ramindra road, and a 900-rai plot in Trad province. In addition, PF owns Uniloft Chiangmai, a dormitory, and six good-quality hotel properties.

Over the next two years, PF's strategy is to focus on landed property developments, sell some land to unload its balance sheet, and divest non-core assets. PF intends to sell four pieces of freehold land worth THB1.5 billion, three pieces of leasehold land, Uniloft Chiangmai, its total stake in the Royal Orchid Sheraton Hotel and Towers, and a 49% stake in Hyatt Regency Sukhumvit. TRIS Rating has incorporated PF's plan to sell the Royal Orchid Sheraton Hotel and Towers as well as land plots located in Chaengwattana, Krunghtep-Kreetha, and Ramkamhaeng in our base case. The proceeds from its asset sales, if successful, should bring down PF's debt to capitalization ratio to below 65%. However, its FFO to total debt ratio may not meet our trigger level of 3% if the company's operating performance fails to return to normal levels.

Liquidity tightens

PF's liquidity remains tight. As of June 2020, debt coming due over the next 12 months amounted to THB8.5 billion, consisting of THB5.5 billion in debentures, THB1.7 billion in short-term borrowings, THB1.0 billion in project loans, and THB0.3 billion in financial lease. PF's sources of funds comprised cash on hand of THB2.4 billion and undrawn unconditional committed credit facilities of THB0.5 billion. In addition, PF had unencumbered land plots worth THB3.8 billion at book value and remaining stock units worth THB6.1 billion in debt-free projects, which can be used as collateral for new loans, if needed.

PF plans to refinance its maturing bonds by new bond issuance. However, due to uncertainty concerning investor demand in the capital market, we view that PF is exposed to significant rollover risk. To mitigate this risk, PF plans to seek bank loans in advance as an alternative source of funds.

BASE-CASE ASSUMPTIONS

These are the key assumptions in TRIS Rating's base-case forecast for PF's operations during 2020-2022:

- PF to slow down new project launches this year, then open new landed property projects, both owned and under JVs, worth THB10 billion per annum as well as new condominium projects worth THB2 billion per annum during 2021-2022.
- Annual budget for land acquisition of THB1-THB2 billion.
- Revenue from hotel business to plunge by around half this year and to gradually revive in 2021. We expect revenue from hotel operations to reach THB2.7 billion in 2022.

- Total operating revenues to decline to THB13 billion this year, improving to THB15-THB16 billion per annum during 2021-2022.
- PF to lower its land burden and divest non-core assets over the next 12 months.

RATING OUTLOOK

The “stable” outlook reflects our expectation that PF’s financial profile will not deteriorate further from its current level. We expect its operating performance to gradually recover over the next two years.

RATING SENSITIVITIES

PF’s ratings and/or outlook could be revised downward should there be clear signs that lead us to believe the company’s operating performance and/or financial profile are heading for a deeper deterioration than expected. We could also lower the ratings if PF’s liquidity depletes faster than we expect. On the contrary, the credit upside would materialize if its operating performance recovers to the pre-COVID level and its financial profile improves, such that the debt to capitalization ratio stays below 65% and the FFO to total debt ratio stays above 3%, on a sustainable basis.

COMPANY OVERVIEW

PF was founded in 1985 by Mr. Chainid Adhyanasakul, and listed on the Stock Exchange of Thailand (SET) in 1993. The company focuses on the middle- to high-income segments of the residential property market in the Bangkok suburbs. PF offers landed property units under the Lake Legend, Perfect Masterpiece, Perfect Residence, Perfect Place, Perfect Park, Modi Villa, and The Metro brands. Its landed property products range in price from THB2 million to THB80 million per unit. Condominium units are sold under the Hyde, Yu Kiroro, The Sky, Metro Sky, Metro Luxe, Metro Park, Bella Costa, I Condo, and Yu Ruay brands, with selling prices ranging from THB40,000 to THB400,000 per square meter (sq.m.). In 2018, PF set up several JVs with partners; HKL Thai Development Co., Ltd., Sekisui Chemical Co., Ltd., and Sumitomo Forestry Co., Ltd., to enlarge its residential portfolio. Apart from its core business, PF operates six hotels, five located in Thailand and one in Japan, one community mall, and 17 discount store branches. PF has also invested in the wind and solar energy businesses through JVs.

Revenue from the residential property business (including landed property, condominiums, and land plot sales) contributed 80%-83% of total revenue from sales and services during 2016 through the first six months of 2020. The revenue contribution from the hotel business increased to 18% in 2019 and 16% in the first half of 2020 from 14%-15% during 2016-2018, following the acquisition of Royal Orchid Sheraton Hotel and Towers in mid-2018 and the opening of Hyatt Regency Sukhumvit in late-2018. The revenue contribution from the rental and services remained negligible.

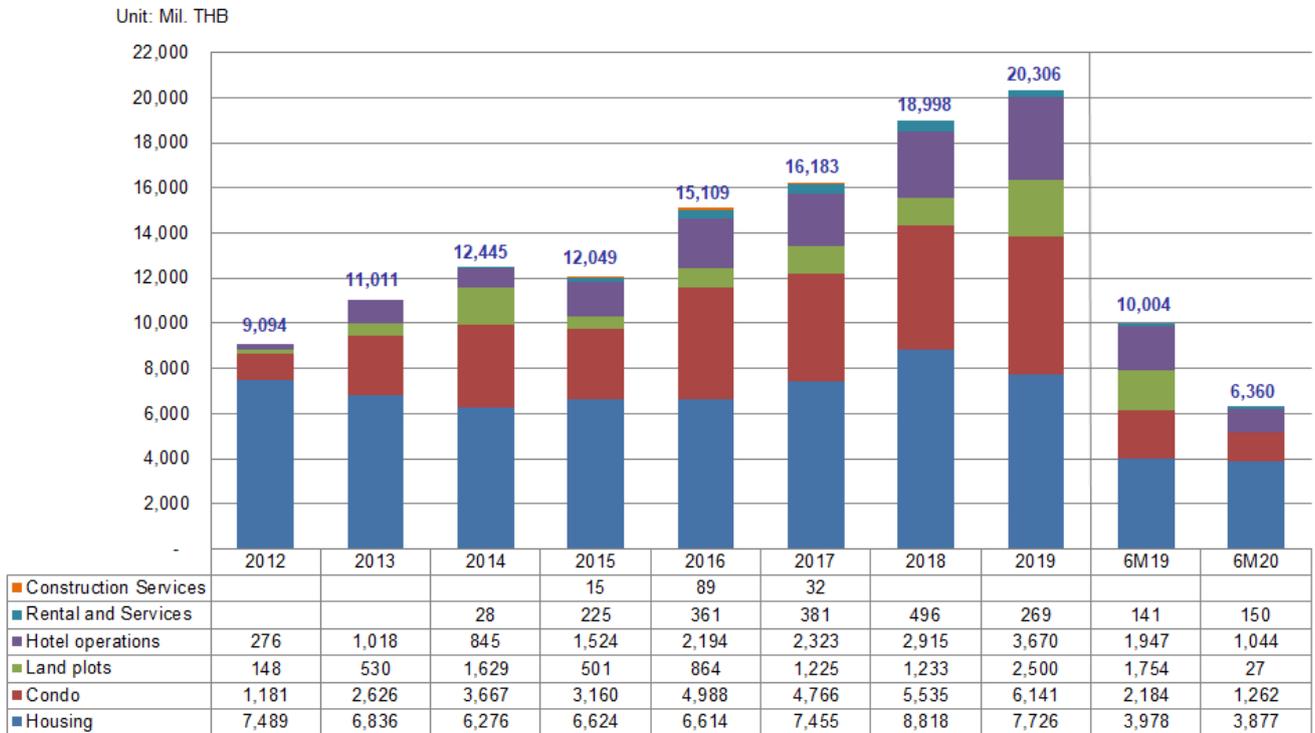
KEY OPERATING PERFORMANCE

Chart 1: Presales Performance



Source: PF

Chart 2: Revenue from Sales and Services Breakdown



Source: PF

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS*

Unit: Mil. THB

	Jan-Jun 2020	-----Year Ended 31 December -----			
		2019	2018	2017	2016
Total operating revenues	6,682	20,758	19,290	16,426	15,425
Earnings before interest and taxes (EBIT)	276	2,828	2,127	1,544	1,670
Earnings before interest, taxes, depreciation, and amortization (EBITDA)	878	3,745	3,018	2,390	2,511
Funds from operations (FFO)	(259)	990	786	407	765
Adjusted interest expense	1,173	2,435	1,902	1,763	1,461
Real estate development investments	31,212	31,822	32,780	29,985	31,925
Total assets	55,899	59,065	57,566	47,684	48,790
Adjusted debt	35,553	34,834	35,187	27,399	29,314
Adjusted equity	14,986	15,688	15,474	15,031	13,937
Adjusted Ratios					
EBITDA margin (%)	13.14	18.04	15.64	14.55	16.28
Pretax return on permanent capital (%)	2.06 **	5.06	4.15	3.35	3.90
EBITDA interest coverage (times)	0.75	1.54	1.59	1.36	1.72
Debt to EBITDA (times)	16.56 **	9.30	11.66	11.46	11.67
FFO to debt (%)	(0.51) **	2.84	2.23	1.48	2.61
Debt to capitalization (%)	70.35	68.95	69.46	64.57	67.78

* Consolidated financial statements

** Annualized with trailing 12 months

RELATED CRITERIA

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

Property Perfect PLC (PF)

Company Rating:	BB
Issue Ratings:	
PF17PA: Bt447.7 million subordinated capital debentures	B
PF18PA: Bt60.3 million subordinated capital debentures	B
Rating Outlook:	Stable

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