

THAILAND PRIME PROPERTY FREEHOLD AND LEASEHOLD REAL ESTATE INVESTMENT TRUST

No. 71/2023
28 April 2023

CORPORATES

Company Rating:	BBB+
Issue Rating:	
Senior unsecured	BBB+
Outlook:	Stable

Last Review Date: 29/04/22

Company Rating History:

Date	Rating	Outlook/Alert
29/04/22	A-	Negative
26/09/19	A-	Stable

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RATIONALE

TRIS Rating downgrades the company rating on Thailand Prime Property Freehold and Leasehold Real Estate Investment Trust (TPRIME or “trust”) and the rating on its senior unsecured debentures to “BBB+” from “A-” and revises the outlook to “stable” from “negative”. The rating downgrades reflect TPRIME’s weakening operating performance amid the rising pressure on the trust’s occupancy and rental rates as a huge supply of new office space in the central business district (CBD) area is anticipated in the coming years. The ratings continue to be constrained by portfolio concentration risk in terms of assets, tenants, and lease expiry. Nonetheless, the ratings are supported by TPRIME’s acceptable cash flow protection, low financial leverage, and adequate liquidity.

KEY RATING CONSIDERATIONS

Weakening credit profile from deteriorating performance

TPRIME’s downward trend in operating performance from lower occupancy and rental rates impaired the trust’s revenue and earnings in 2021-2022. The average occupancy rate (OR) of “Exchange Tower” (EXCHANGE) shrank from above 90% in 2017-2020 to around 75%-80% during 2021-2022. The OR of “Mercury Tower” (MERCURY) also declined from above 90% in 2018-2020 to 79% at the end of 2022. Although the trust lowered its rental rates in 2022 in an effort to attract new tenants and retain existing tenants, the OR of both buildings still fell below the industry average of 82% for grade-A CBD office buildings.

A deterioration in occupancy and rental rates caused TPRIME’s annual revenue to decline steadily from more than THB900 million during 2018-2020 to THB811 million in 2021 and THB769 million in 2022. The trust’s profitability also weakened. Its earnings before interest, taxes, depreciation, and amortization (EBITDA) margin contracted from 72% in 2020 to 66% in 2021 and 61% in 2022, making its EBITDA drop below THB500 million for the first time.

Future performance challenged by huge supply

We hold the view that the trust’s OR and rental rate will remain under pressure in the medium term as demand has not fully recovered while a huge supply influx is anticipated. According to CB Richard Ellis (CBRE), around 450,000-500,000 square meters (sq.m.) of new office space per year is expected to enter the market in 2023-2024. More than half of the new supply will be categorized as grade-A CBD office buildings. The excess supply has resulted in declining rental rates since 2021. Rental rates for grade-A CBD office buildings dropped by 8% year-on-year (y-o-y) to THB1,040 per sq.m. per month on average in 2022.

Our base-case scenario forecasts TPRIME’s rental rates to decline by 1%-3.5% y-o-y with OR of both buildings in the 75%-82% range over the next three years. We expect the trust’s operating revenue should stay in the THB700-THB790 million range in 2023-2025. Its EBITDA should remain around THB400-THB480 million with an EBITDA margin of around 60% over the forecast period. Any material further deviation from our expectations caused by either unfavorable market sentiment or the trust’s mounting business risk could lead to a downward revision of the rating.

Ratings constrained by portfolio concentration risk

We view that TPRIME's asset portfolio remains exposed to significant concentration risk in terms of the number of properties, tenants, and lease expiry. The trust's rental income and EBITDA hinge 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. Therefore, unfavorable operating results in any single asset could considerably impact the overall performance of the trust. In terms of tenants, the top-ten tenants accounted for 53% of total occupied area for EXCHANGE and 58% of total leased area for MERCURY. The top-ten tenants of each building contributed 49% of rental and services income for EXCHANGE and 51% for MERCURY. The largest tenant occupied 6% of the trust's total leased area and contributed 5% of its rental and services income.

In addition, most of TPRIME's lease contracts have a three-year lease term. This exposes the trust to some degree of lease renewal risk. As of December 2022, 19% of the existing contracts based on occupied area will expire in 2023, 35% in 2024, and 46% in 2025. Lease contract expirations are highly concentrated in 2024 and 2025 since the lease agreements of 10 major tenants of both buildings will expire within the same period. The renewal rates for EXCHANGE and MERCURY were 75%-85% in 2021-2022. However, a massive influx of new office supply has raised our concerns over the renewal rates of both buildings in the coming years.

Cash flow protection softens, but remains acceptable

Despite an expected decrease in the revenue and earnings base, we anticipate TPRIME's cash flow protection to remain acceptable, thanks to its low financial leverage. The trust's softening revenue and profitability caused its adjusted net debt to EBITDA ratio to increase to 3.1-3.5 times in 2021-2022, from below 3 times in 2018-2020. The EBITDA interest coverage ratio also declined, falling to 8-8.5 times in 2021-2022 from 11 times in 2020. However, the trust's low financial leverage with the debt to capitalization ratio of around 20% helps mitigate the deterioration in its financial risk profile.

Looking forward, we project TPRIME's earnings to decline amid the expected drop in revenues and profit margins. In addition, interest rate hikes may result in higher funding costs on its bank loans. We expect the trust's adjusted net debt to EBITDA ratio to increase to 3.5-4 times and its EBITDA interest coverage ratio could decline to 5.5-7 times in 2023-2025. Currently, the trust has no concrete plans for new asset acquisition. Thus, we estimate the debt to capitalization ratio to stand at the current level over the forecast period.

Adequate liquidity

We assess TPRIME's liquidity as adequate for the next 12 months. The trust's sources of liquidity as of December 2022 include cash on hand of THB710 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. The trust's high-quality unencumbered assets can also be used as collateral for bank loans, if needed. The market value of its unencumbered assets at the end of 2022 was THB8.71 billion. As of December 2022, TPRIME had THB2.05 billion in outstanding debentures, including THB1 billion due in 2023 and THB1.05 billion due in 2027. TPRIME already refinanced its matured debentures due in January 2023 with 3-year term loans. Hence, the trust has no debt due from the rest of this year through 2025.

The financial covenants on TPRIME's bank loans require the trust to maintain its loan to fair value of total assets (LTV) ratio, excluding lease liability, below 35% and the reported interest-bearing debt to reported EBITDA ratio below 6 times. At the end of 2022, the LTV ratio was 21.6% and the reported interest-bearing debt to reported EBITDA ratio was 4.4 times. We believe the trust should have no problems complying with the financial covenants over the next 12 to 18 months.

BASE-CASE ASSUMPTIONS

Here are our key base-case assumptions for TPRIME's operations during 2023-2025:

- OR for both office buildings in the 75%-82% range
- Rental rates decline by 1%-3.5% y-o-y
- EBITDA margin drops to around 60%
- No new asset acquisition

RATING OUTLOOK

The "stable" outlook reflects our expectation that TPRIME will be able to deliver its operating performance as targeted while its financial profile should not materially further deteriorate from our base-case forecast.

RATING SENSITIVITIES

TPRIME's ratings and/or outlook could be revised downward if the industry risk evolves in a way that leads us to believe that the mismatch between supply and demand in office space could severely impact the trust's operating results and financial profile. A significant decline in OR and/or rental rates from the current level and an increase in the adjusted net debt to EBITDA ratio to a level above 5.5 times could trigger a downward revision of the rating/outlook.

On the other hand, an upward rating revision would materialize if the trust can deliver stronger-than-expected operating and financial results, with OR recovering to 85%-90% on a sustained basis and rental rates showing a sign of improvement.

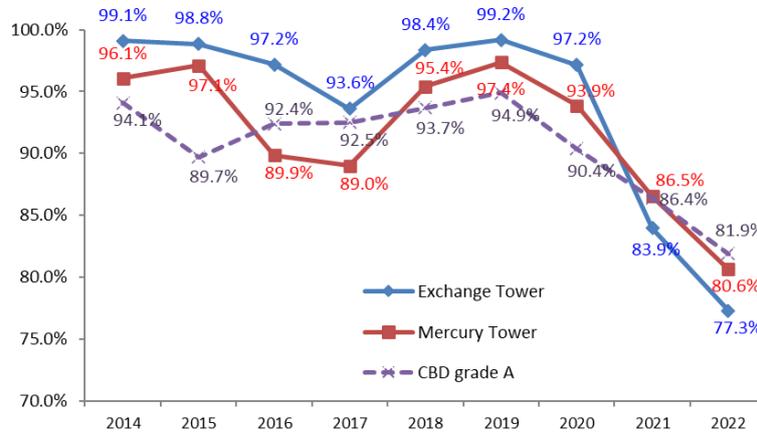
COMPANY OVERVIEW

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, an investment holding company, 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) Co., Ltd. for EXCHANGE and Jones Lang LaSalle Management Co., Ltd. for MERCURY.

The trust's assets comprise two office buildings, EXCHANGE and MERCURY, with a total net leasable area of 67,631 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 2022, the fair value of TPRIME's assets was THB8.71 billion. The trust's rental and service income was THB767 million in 2022. EXCHANGE generated about 65% of the rental and service income and the rest came from MERCURY.

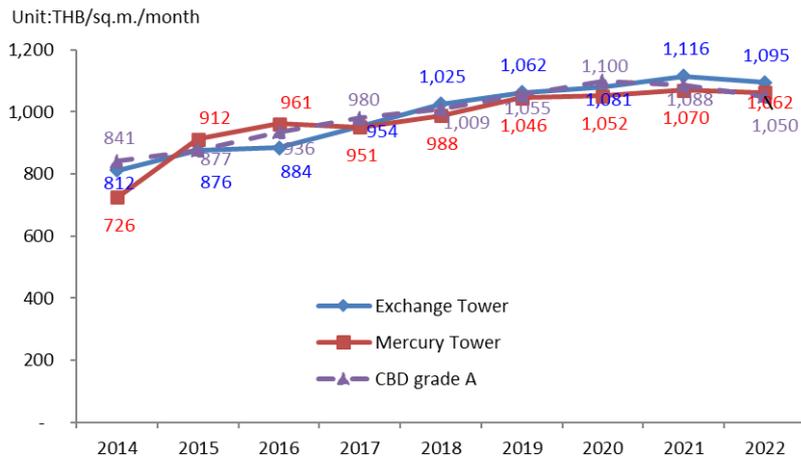
KEY OPERATING PERFORMANCE

Chart 1: Occupancy Rate



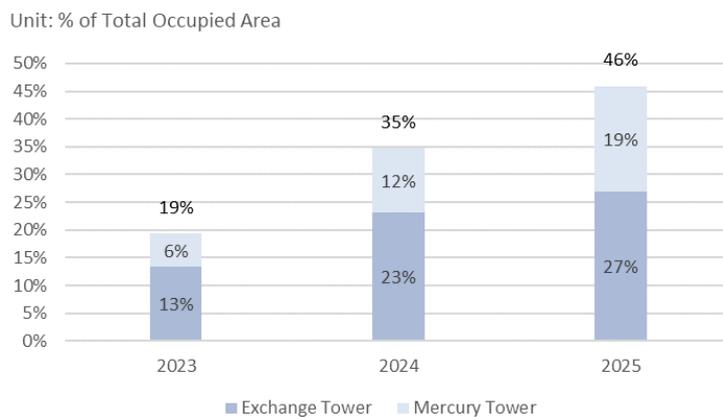
Note: From 2020, OR as average occupancy rate
Sources: TPRIME and CB Richard Ellis (CBRE)

Chart 2: Rental Rate



Source: TPRIME and CB Richard Ellis (CBRE)

Chart 3: Lease Expiry



Source: TPRIME

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS*

Unit: Mil. THB

	-----Year Ended 31 December -----				
	2022	2021	2020	2019	2018
Total operating revenues	769	811	923	979	930
Earnings before interest and taxes (EBIT)	466	499	621	611	533
Earnings before interest, taxes, depreciation, and amortization (EBITDA)	470	532	663	658	580
Funds from operations (FFO)	357	404	519	496	428
Adjusted interest expense	58	62	60	87	88
Investments in properties and leasehold rights over					
Properties at fair value	8,712	8,760	8,666	8,125	7,904
Total assets	9,488	9,528	9,478	8,972	8,721
Adjusted debt	1,649	1,673	1,517	1,559	1,604
Adjusted equity	6,751	6,788	6,839	6,420	6,160
Adjusted Ratios					
EBITDA margin (%)	61.13	65.63	71.90	67.24	62.31
Pretax return on permanent capital (%)	5.11	5.48	7.04	7.22	6.52
EBITDA interest coverage (times)	8.05	8.53	10.98	7.53	6.59
Debt to EBITDA (times)	3.51	3.15	2.29	2.37	2.77
FFO to debt (%)	21.67	24.15	34.22	31.78	26.66
Debt to capitalization (%)	19.63	19.78	18.15	19.54	20.66

* Consolidated financial statements

RELATED CRITERIA

- Corporate Rating Methodology, 15 July 2022
- Key Financial Ratios 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

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

Company Rating:	BBB+
Issue Rating:	
TPRIME271A: THB1,050 million senior unsecured debentures due 2027	BBB+
Rating Outlook:	Stable

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