

# DUSIT THANI FREEHOLD AND LEASEHOLD REAL ESTATE INVESTMENT TRUST

No. 130/2020  
28 August 2020

## CORPORATES

**Company Rating:** BBB-  
**Outlook:** Negative

**Last Review Date:** 27/03/20

### Company Rating History:

Date	Rating	Outlook/Alert
27/03/20	BBB	Alert Negative
19/12/19	BBB	Stable

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## RATIONALE

TRIS Rating removes the “CreditAlert” with “negative” implication on Dusit Thani Freehold and Leasehold Real Estate Investment Trust (DREIT or trust) and downgrades the company rating on DREIT to “BBB-”, from “BBB”. At the same time, TRIS Rating assigns a “negative” outlook to the rating.

The rating action follows the rating downgrade on its sponsor, Dusit Thani PLC (DTC), which was downgraded to “BBB-” with a “negative” rating outlook. TRIS Rating views that DREIT’s credit profile relies, in large part, on DTC’s credit quality as DTC is the sole renter and the only source of cash flow to DREIT.

The “negative” outlook reflects the high degree of uncertainty on the revival of the hospitality industry as the Coronavirus Disease 2019 (COVID-19) pandemic situation keeps evolving. We expect the hospitality industry will continue to be under stress throughout 2020-2021 as travel restrictions are likely to continue for an extended period of time. The economic fallout from the pandemic could also be a deterring force hindering the revival of hospitality businesses.

## KEY RATING CONSIDERATIONS

### Significant impact from COVID-19 on operating performance of the trust’s hotel properties

Hospitality is one of the sectors severely affected by the fallout of the COVID-19 pandemic. Travel restrictions imposed across countries have caused a deep slump in the hospitality sector worldwide, particularly in the second quarter of 2020. Although many countries have begun easing lockdown measures and reopened their borders to some extent, some forms of travel restrictions will likely remain for an extended period. Concerns over air-travel safety may also hinder the resumption of long-haul international travel for the next several quarters. Apart from health concerns, the drop in air transport capacity could also be a deterring factor as the harshly hit aviation industry could take some time to recover. Adding the impact of the global recession to the sluggish travel demand, we assess it will take at least 24 months for the demand for hospitality services to recover to pre-COVID-19 levels.

We project average revenue per available room (RevPAR) of DREIT’s properties to drop by around 65% in 2020. Despite the improving trend, we project RevPAR in 2021 to stay around 20% below the 2019 level and RevPAR in 2022 to be about 10% lower than the 2019 level. These projections are based on our view that “Dusit Thani Hua Hin” will recover faster than the other three properties as domestic travelers make up a considerable proportion of the guest profile at Dusit Thani Hua Hin, while the other three properties rely mainly on international travelers.

### Revenue downside protected by minimum rent scheme under sublease agreements with DTC

Revenue downside risk of the trust is limited by a committed minimum rental fee scheme. The laws governing real estate investment trusts (REIT) prohibit a REIT from operating a hotel. Because of this, DREIT leases “Dusit Thani Laguna Phuket” and “Dusit D2 Chiangmai”, and subleases Dusit Thani Hua Hin to Dusit Management Co., Ltd. (DMCO). DREIT also subleases “Dusit Thani Maldives” to Dusit Maldives Management Pvt., Ltd. (DMM). Both DMCO and

DMM are subsidiaries of DTC.

DMCO pays DREIT a fixed rental fee and a variable rental fee. The fixed portion of the rent is reset each year depending on the actual operating results of each hotel, but is not less than THB205 million per year. The variable portion of the rent is 85% of what DMCO makes after deducting hotel operating expenses and the fixed portion of the rent.

For Dusit Thani Maldives, DMM rents the hotel for 21 years of operation. DMM pays a minimum fixed rental fee of USD7 million per year. The variable portion of the rent is 90% of what DMM makes after deducting hotel operating expenses and the fixed portion of the rent.

However, as DTC is the sole renter and the only source of cash flow to DREIT, the credit quality of DTC is a key determinant of the rating on the trust.

#### **Only minimum fixed rent expected in 2020 and 2021**

We expect that DREIT will receive only the minimum fixed rental of about THB430 million per year during 2020-2021 after taking into account the expected distressed revenues and earnings at the property level. We expect DREIT to receive rent of around THB455 million in 2022. The rental income will translate into earnings before interest, tax, depreciation, and amortization (EBITDA) of THB385 million per annum during 2020-2021 and around THB410 million in 2022.

According to the rental agreement, if the hotel industry is significantly affected by adverse operating conditions which impact the trust's asset performance, DTC may request a postponement of the rental payment. However, any postponement is subject to the trust's approval.

As the trust's properties have been severely affected by the COVID-19 pandemic, DTC requested to postpone the rental payment of Dusit Thani Maldives from April to July 2020 and of the three properties in Thailand from May to July 2020.

With the easing of lockdown measures and the spread of virus is largely under control domestically, Dusit Thani Hua Hin reopened in June 2020 followed by Dusit Thani Maldives in August 2020. Dusit Thani Laguna Phuket and Dusit D2 Chiangmai are to reopen in September 2020. DTC is to resume rental payments for all four properties in August 2020 and will pay all the deferred rental payments within this year. However, if the depth and the length of the COVID-19 impact are worse than expected, it is possible that more rental payments could be postponed, once again halting DREIT's cash flow.

#### **Small asset portfolio with concentration risk**

DREIT's credit profile takes into consideration its small asset portfolio in terms of assets and earnings sizes. Its assets comprise four hotels in key but highly competitive tourist destinations in Thailand and the Maldives with around 60% of rental income coming solely from the Maldives asset.

As of June 2020, the fair value of DREIT's properties was THB7.18 billion. At the asset level, Dusit Thani Laguna Phuket, Dusit Thani Hua Hin, and Dusit D2 Chiangmai, together, generated revenue of THB254 million and EBITDA of THB15.9 million in the first half of 2020 while Dusit Thani Maldives generated USD6.2 million in revenue and USD1.6 million in EBITDA.

#### **Acceptable leverage**

DREIT's leverage has risen due to the acquisition of Dusit Thani Maldives and renovation expenditures. DREIT completed the acquisition of Dusit Thani Maldives in September 2019 for THB2.36 billion. Funding sources comprised new equity from unit holders of THB1.78 billion with the balance funded by debt. At the end of June 2020, DREIT's adjusted debt was THB1.78 billion. The hotel renovation budget is estimated to be around THB200 million in 2020, around THB20 million in 2021, and around THB70 million in 2022. During 2020-2022, TRIS Rating expects DREIT's adjusted debt to capitalization ratio to range from 26%-28%. The adjusted debt to EBITDA ratio is expected to be 5-5.5 times.

#### **Manageable liquidity**

We consider DREIT's liquidity position to be manageable during the remainder of 2020 through 2021. The primary sources of funds are expected funds from operations (FFO) of around THB290 million per annum during 2020-2021, cash and cash equivalents on hand of THB204 million as of June 2020, and available credit facilities of THB256 million. As DREIT has no debt repayments until 2024, its liquidity sources are expected to cover its needs, which are mainly capital expenditure of around THB165 million in the second half of 2020 and THB20 million in 2021. The trust plans to pay dividends to unit holders of THB125 million in the second half of 2020 and around THB250 million in 2021.

#### **BASE-CASE ASSUMPTIONS**

- Average hotel RevPAR to drop by around 65% in 2020. RevPAR in 2021 to stay around 20% below the 2019 level and in 2022 around 10% lower than the 2019 level.

- DREIT to receive only the minimum fixed rental during 2020-2021 of around THB430 million per year and rental revenue of THB455 million in 2022.
- EBITDA of THB385 million per annum during 2020-2021 and THB410 million in 2022.
- Hotel renovation budget of THB200 million in 2020, around THB20 million in 2021, and around THB70 million in 2022.

**RATING OUTLOOK**

The “negative” outlook reflects the high degree of uncertainty with respect to the pace of business recovery amid the fluid pandemic situation and the economic fallout from the pandemic.

**RATING SENSITIVITIES**

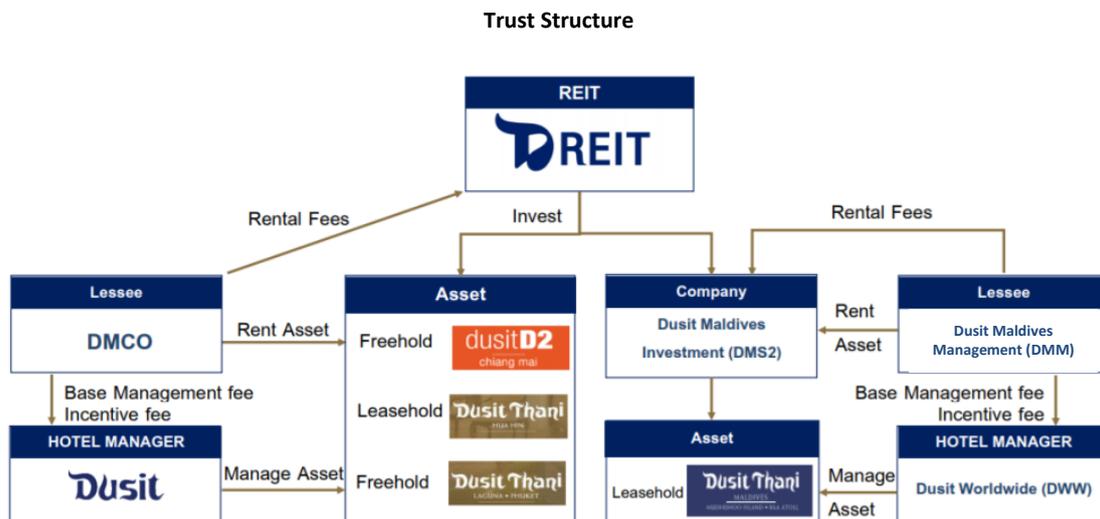
The outlook could be revised to “stable” if the operating performance of the trust’s properties steadily recovers and the trust maintains sufficient liquidity to weather any adverse conditions. TRIS Rating could revise the rating downward if the effects of the COVID-19 pandemic turn out to be more severe than expected. We could also lower the rating if the liquidity of DREIT is depleted faster than expected. In addition, as DTC is DREIT’s only source of cash flow, a material change in DTC’s credit profile could have an impact on the rating on DREIT.

**COMPANY OVERVIEW**

DREIT is a non-redeemable and indefinite REIT. It was established on 29 November 2017 and received assets and liabilities transferred from Dusit Thani Freehold and Leasehold Property Fund (DTCPF) on 8 December 2017. DREIT was listed on the Stock Exchange of Thailand (SET) on 15 December 2017. As of April 2020, the major shareholders of the trust consisted of DTC with a stake of 30.02% and the Social Security Office (SSO) with 25.41%. The REIT manager is Dusit Thani Properties REIT Co., Ltd., a subsidiary of DTC.

DREIT has a policy to generate benefits from hotel investments by leasing assets and subleasing leasehold rights to DMCO, a subsidiary of DTC. The property portfolio currently comprises four hotels, Dusit Thani Laguna Phuket, Dusit Thani Hua Hin, Dusit D2 Chiangmai, and Dusit Thani Maldives. As of June 2020, the fair value of DREIT’s properties was THB7.18 billion.

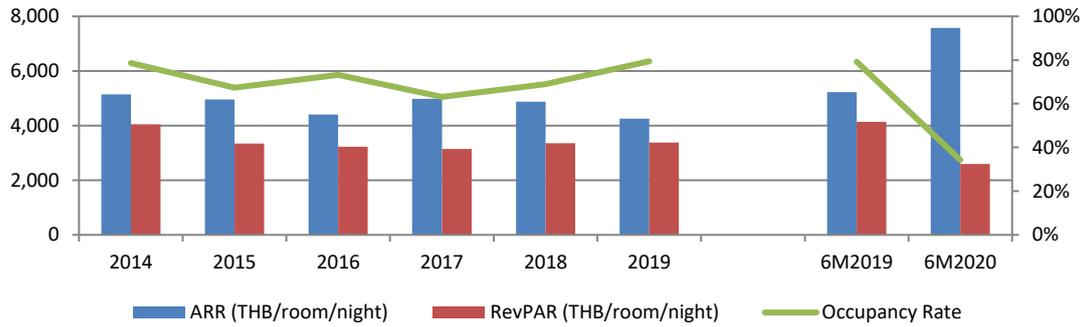
At the asset level, Dusit Thani Laguna Phuket, Dusit Thani Hua Hin, and Dusit D2 Chiangmai, together, generated revenue of THB253.7 million and EBITDA of THB15.9 million in the first half of 2020 while Dusit Thani Maldives generated USD6.2 million in revenue and USD1.6 million in EBITDA.



Source: DREIT

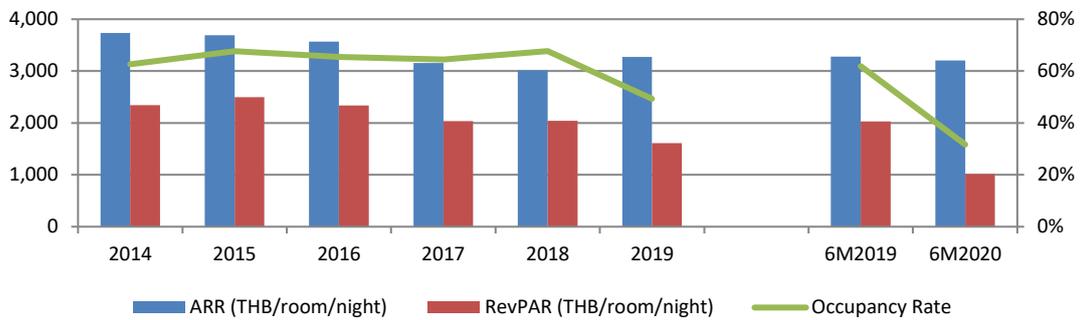
**KEY OPERATING PERFORMANCE**

**Chart 1: Average Room Rate and Occupancy Rate of Dusit Thani Laguna Phuket**



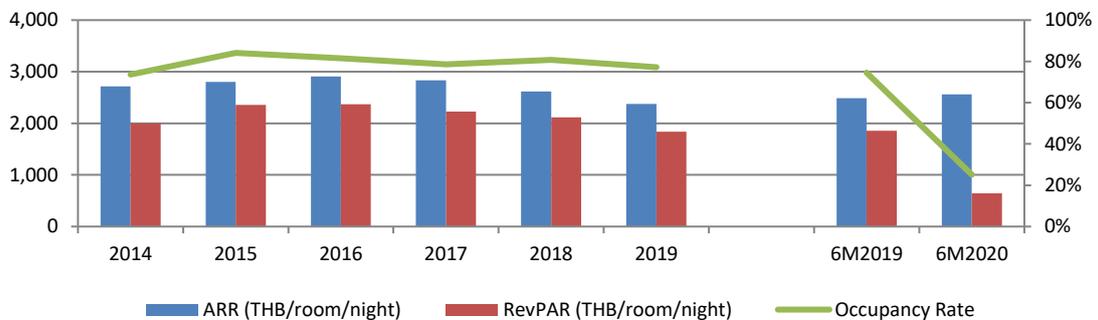
Source: DREIT

**Chart 2: Average Room Rate and Occupancy Rate of Dusit Thani Hua Hin**



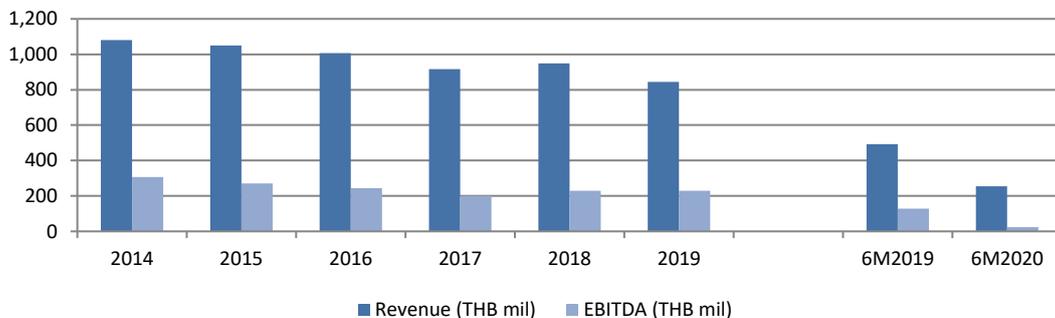
Source: DREIT

**Chart 3: Average Room Rate and Occupancy Rate of Dusit D2 Chiangmai**



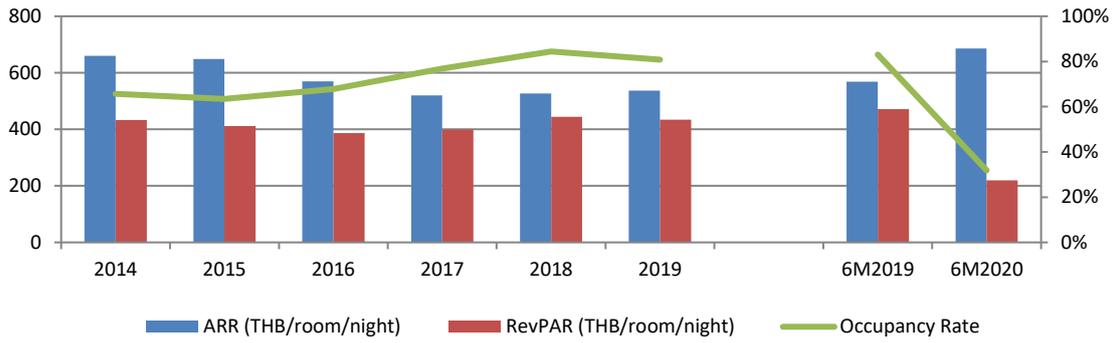
Source: DREIT

**Chart 4: Performance of Three Hotels in Thailand (Dusit Thani Laguna Phuket, Dusit Thani Hua Hin, and Dusit D2 Chiangmai)**



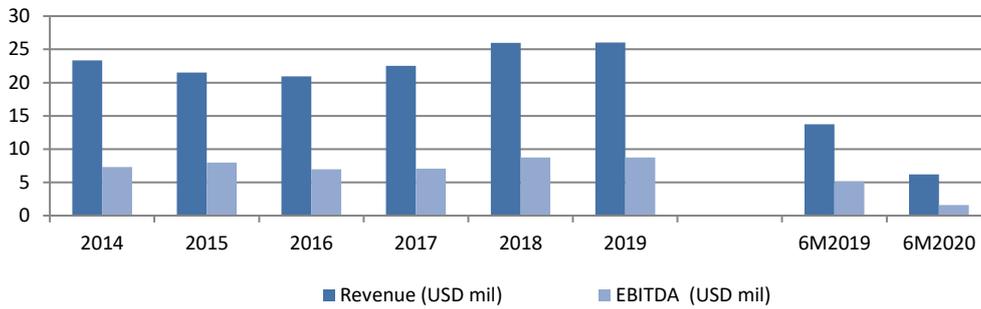
Source: DREIT

**Chart 5: Average Room Rate and Occupancy Rate of Dusit Thani Maldives**



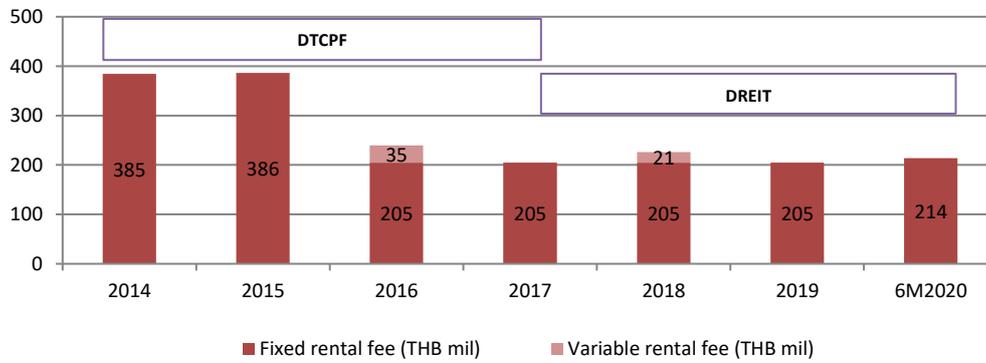
Source: DREIT

**Chart 6: Performance of Dusit Thani Maldives**



Source: DREIT

**Chart 7: Rental Revenue of DREIT**



Source: DREIT

## FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS

Unit: Mil. THB

	---Year Ended 31 December ---		
	Jan-Jun 2020	2019	2018
Total operating revenues	214	288	226
Earnings before interest and taxes (EBIT)	186	263	207
Earnings before interest, taxes, depreciation, and amortization (EBITDA)	186	263	207
Funds from operations (FFO)	147	209	186
Adjusted interest expense	37	46	22
Capital expenditures	36	2,561	173
Total assets	7,538	6,977	4,382
Adjusted debt	1,778	1,821	564
Adjusted equity	5,524	5,401	3,728
<b>Adjusted Ratios</b>			
EBITDA margin (%)	86.53	91.19	91.51
Pretax return on permanent capital (%)	5.67	4.53	4.82
EBITDA interest coverage (times)	5.01	5.67	9.62
Debt to EBITDA (times)	5.21	6.92	2.72
FFO to debt (%)	14.77	11.49	32.93
Debt to capitalization (%)	24.35	25.21	13.13
Loan to fair value of total assets (%)	26.29	21.33	13.67

## RELATED CRITERIA

- Rating Methodology – Corporate, 26 July 2019
- Key Financial Ratios and Adjustments, 5 September 2018
- Real Estate Investment Trust, 12 October 2016

## Dusit Thani Freehold and Leasehold Real Estate Investment Trust (DREIT)

<b>Issuer Rating:</b>	BBB-
<b>Rating Outlook:</b>	Negative

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