
Fitch Places Thailand's TREIT on Rating Watch Positive Upon Planned Merger

Fitch Ratings-Bangkok-06 October 2017: Fitch Ratings (Thailand) Limited has placed TICON Freehold and Leasehold Real Estate Investment Trust's (TREIT) 'A-(tha)' National Long-Term Rating and national senior unsecured rating on Rating Watch Positive (RWP). This follows an announcement by TICON Industrial Connection Public Company Limited (TICON) that it will merge its group-sponsored property funds - TICON Property Fund, TPARK Logistics Property Fund and TICON Industrial Growth Leasehold Property Fund - under TREIT. The property funds' assets and liabilities will be exchanged via issuance of TREIT trust units and cash payments, which will be financed by debt.

The RWP reflects Fitch's expectation that the merger will transformatively increase TREIT's scale - by more than four times - and lead to greater tenant diversification. However, we do not expect a significant change in TREIT's financial profile, as the company aims to maintain its gross debt/total assets at about 30%. The RWP should be resolved upon transaction approval by the unitholders of all related property funds and REITs, including the asset and liability transfers, within the designated timeframe; that is, by 31 December 2017. This timeframe may be extended along with any extension of government-granted conversion-related tax and fee incentives, which could cause the RWP resolution take longer than the typical six-month period.

KEY RATING DRIVERS

Deal Transforms Scale: The transaction, if completed, will enlarge TREIT's property portfolio to THB30.8 billion, from THB7.3 billion at end-June 2017. Tenant diversification is also likely to improve, with the 10 largest tenants contributing around 22% of total revenue, from 50% previously. However, the average term to lease maturity would be shortened, with the proportion of leases expiring within three years increasing to 73.9%, from 47.2%. Fitch expects the occupancy rate of the enlarged portfolio to remain at 78%-80% after the conversion.

Weaker-than-Expected Occupancy: Fitch expects TREIT's average occupancy rate, based on its current portfolio, to improve in line with our forecast economic recovery and easing oversupply in Thailand's eastern seaboard. However, the 78% rate at end-June 2017 was weaker than we expected and at the same level as at end-2016. TREIT's average lease-term-to-maturity, at 3.3 years, was unchanged from end-2016, with most contracts expiring in 1H17 being renewed. Moderate renewal risk exists, as 6% of TREIT's lease contracts, based on leased area, expire in 2H17 and another 19% in 2018.

Debt-Funded Growth: The merger will likely see TREIT's leverage, as measured by net debt/investment property value, temporarily decrease to about 17%, from 21% at

end-June 2017. Fitch expects leverage to increase to 28%-30% over the medium term, in accordance with TREIT's financing policy. TREIT had planned to invest up to THB750 million in the assets of other developers in late 2017, with 100% financing via debt, but this is likely to be postponed while it converts all TICON group-sponsored property funds to a REIT.

DERIVATION SUMMARY

TREIT is significantly smaller than WHA Corporation Public Company Limited (BBB+(tha)/Negative), a leading developer of industrial estates and built-to-suit industrial properties for rent in Thailand. TRIET's EBITDA will still be about 50% smaller than that of WHA, even after the proposed investment in the assets of the property funds under the conversion plan. TREIT has higher earning visibility from its property rental business and no development risk exposure, while WHA has large development exposure with project completion risk. About 60% of WHA's EBITDA comes from its industrial land sales business, which is subject to cyclical demand. TREIT has higher EBITDA margins and lower financial leverage than WHA, although leverage may increase in the medium term. Therefore, TREIT is rated higher than WHA.

TREIT is smaller in terms of EBITDA and operating scale against The Siam Cement Public Company Limited (SCC, A(thai)/Positive), Thailand's largest cement and downstream petrochemicals producer, and Siam City Cement Public Company Limited (SCCC, A(thai)/Stable), the country's second-largest cement producer. TREIT has high earning visibility, while SCC and SCCC are exposed to cyclical product demand commodity price fluctuations. TREIT also has a higher EBITDA margin. However, SCC and SCCC have lower financial leverage.

KEY ASSUMPTIONS

Fitch's key assumptions within our rating case for the issuer (excluding the conversion plan) include:

- Additional investment of THB750 million in 2017, with 100% debt financing, and about THB2 billion a year in 2018 - 2019, with 30% debt financing.
- Lease renewal rate of 85%, taking four to six months to seek new lessees in 2017-2019.
- EBITDA margin of 75%-80% in 2017-2019 (1H17: 77%).
- No development or significant maintenance capex over 2017-2019.

RATING SENSITIVITIES

Developments that May, Individually or Collectively, Lead to Positive Rating Action
Fitch expects to resolve the RWP upon transaction closing, which may take longer than six months. Fitch will take positive rating action if :

- investment properties exceeds THB30 billion, with higher granularity in term of tenants and geography;

- the occupancy rate is sustained at over 80%; and
- net debt/investment-property value is sustained at 20%-25% (end-June 2017: 21%), net debt/EBITDA at 3.0x-3.5x (end-June 2017: 3.5x) or FFO fixed-charge coverage at above 3.5x (end-June 2017: 4.5x).

Developments that May, Individually or Collectively, Lead to Negative Rating Action
In the absence of the transaction progressing, the Outlook will revert to Negative.

LIQUIDITY

Comfortable Liquidity: Fitch expects TREIT to have enough liquidity in the next two to three years to comfortably cover interest payments, with EBITDA/interest expense expected at above 4.5x. Minimal maintenance capex is expected for the next two to three years. Liquidity for new investment is likely to be supported by its ability to access the capital market for both debt and equity.

Deal Increasing Secured Debt: TREIT plans to raise secured debt of THB3.8 billion to support the conversion plan. Recovery prospects of unsecured creditors could be jeopardised if secured debt exceeds 2.0x-2.5x of EBITDA, negatively affecting the senior unsecured debt rating.

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Summary of Financial Statement Adjustments

- Net purchase and sale of securities investments are not included in cash flow changes, but is taken as cash and cash equivalent, as all securities investment is via fixed deposit.

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Applicable Criteria

Corporate Rating Criteria (pub. 07 Aug 2017)

National Scale Ratings Criteria (pub. 07 Mar 2017)

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