FitchRatings

10 Jun 2019 | Rating Changed Outlook to Negative

Fitch Revises Ciputra's Outlook to Negative; Affirms at 'BB-'

Fitch Ratings-Singapore/Jakarta-11 June 2019: Fitch Ratings has revised the Outlook on Indonesia-based property developer PT Ciputra Development Tbk (CTRA) to Negative from Stable. At the same time, the agency has affirmed the company's Long-Term Issuer Default Rating at 'BB-'. Fitch Ratings Indonesia has revised PT Ciputra Residence's Outlook to Negative from Stable, and affirmed its National Long-Term Rating at 'A+(idn)'. A full list of the rating actions is at the end of this commentary.

The Outlook revision reflects Fitch's view of heightened risks around CTRA's ability to increase its annual attributable property presales to more than IDR5 trillion in the next one to two years. Fitch views this level of presales as commensurate with a Long-Term IDR of 'BB-'. CTRA reported attributable presales of IDR5 trillion-7 trillion a year in 2013-2017, supported by its established domestic franchise and geographically diverse projects. However, the company's attributable presales fell by around 30% in 2018 to about IDR4 trillion, underperforming most rated peers. Fitch may downgrade CTRA's ratings if its attributable presales do not get back on track towards more than IDR5 trillion by 2021. The rating on PT Ciputra Residence is based on the consolidated profile of its parent, CTRA.

'A' National Ratings denote expectations of low default risk relative to other issuers or obligations in the same country. However, changes in circumstances or economic conditions may affect the capacity for timely repayment to a greater degree than is the case for financial commitments denoted by a higher rated category

KEY RATING DRIVERS

Slow Sales on Deferred Launches: We expect CTRA's attributable presales to decline by 7% to IDR3.7 trillion in 2019. Sales in 2Q19 will remain soft given the long Eid holiday in June 2019, but should recover in 2H19 as we expect new product launches to resume and consumer sentiment to improve. CTRA's attributable presales fell by 30% yoy in 1Q19, mainly due to a lack of new products and weak consumer sentiment ahead of the April 2019 elections. We expect presales growth to accelerate from 2020 as economic performance and business activities are likely to improve. Fitch expects Indonesia's GDP growth to pick up to 5.1% in 2020 and 5.3% in 2021 (2019F: 5%).

Fitch also expects CTRA's significant exposure to the low- to mid-end market, where demand is driven more by first-time home buyers, to help the company to improve its presales in the next few years, as consumers in this space are less sensitive to economic cycles. In 2018, around 40% of CTRA's consolidated presales consisted of products in the low- to mid-end market, which is broadly defined as homes with price tags below IDR1 billion.

Investment Properties Support Financing Flexibility: CTRA has substantial non-development cash flows from its quality investment-property portfolio. These add to the company's cash flows from its core property-development business and give it additional financing flexibility and a more stable source of debt servicing during periods of weak property demand. Sustained deterioration in CTRA's non-development interest cover, measured by non-development gross profit/ net interest expense, to below 1x (2018: 1.6x), may signal tighter financing and operating flexibility, and Fitch may reduce the level of leverage, measured as net debt/adjusted inventory, that could lead to negative rating action from the current 40% for CTRA's 'BB-' IDR (2018: 31%).

We expect CTRA's non-development interest cover to increase to 1.7x by 2023 as we expect occupancy of existing properties to improve and three new shopping malls that the company plans to open in 2020-2022 to generate additional non-development cash flows.

Diversified Portfolio; Established Track Record: CTRA's rating is supported by its strong market position as one of Indonesia's largest and most diversified property developers by product, geography and segmentation. It has an established track record, sizeable land bank, and quality assets. The company has 75 residential and commercial projects across 33 Indonesian cities. The group has multiple revenue streams from various segments of the property market, as well as commercial and investment properties including shopping malls, hotels, hospitals, office towers and golf courses.

Sizeable Land Bank: CTRA had around 2,334 hectares of land bank at end-2018, which is spread across the country, with sizeable presence in the main urban areas of Greater Jakarta and Greater Surabaya. The large land bank ensures project longevity, especially when land prices are rising. In addition, the Ciputra group also jointly develops projects with land owners on a profit- or revenue-sharing basis. This helps the group expand its operational scale while limiting the balance-sheet burden. We expect CTRA to provide support to JVs to the extent of its shareholdings, given the reputational risk, and hence we have proportionately consolidated the key financials of major subsidiaries when computing CTRA's financial metrics.

Rating Based on Consolidated Profile: CTRA and its subsidiaries have moderate overall intra-group

operational and legal linkages that stem from comfortable access to cash within the group, common shareholders and board members among the group companies, and a negative pledge provision in the documents for CTRA's Singapore dollar bond that covers all its principal subsidiaries. There are also risks to the overall reputation of the group from the use of the 'Ciputra' brand. Fitch believes these linkages give CTRA strong operational control over its subsidiaries and therefore they operate as a single entity

DERIVATION SUMMARY

CTRA's rating on the international scale may be compared with those of PT Pakuwon Jati Tbk (BB/Stable), PT Bumi Serpong Damai Tbk (BSD; BB-/Stable), KWG Group Holdings Limited (BB-/Stable), PT Modernland Realty Tbk (B/Stable) and PT Alam Sutera Realty Tbk (B/Stable).

Pakuwon is one of Indonesia's leading mixed-use property developers with the majority of its operating cash flows from its large investment property portfolio. Pakuwon is rated higher than CTRA because of its superior non-development income base and more conservative capital structure, which lead to significantly stronger non-development interest cover. Pakuwon's higher rating is also supported by wider profit margins and stronger free cash flow (FCF).

Fitch believes BSD and CTRA have similar business risk profiles, with comparable property presales as the two largest developers in Indonesia. Both companies have strong track records in the domestic property market and benefit from added financial flexibility from their strong non-development property cash flows. Therefore both companies can maintain similar leverage of around 40% for their 'BB-' Long-Term IDRs. BSD is more geographically concentrated than CTRA, with the majority of its presales from its mature BSD City township. However, BSD's presales proved more resilient than CTRA's during the 2018 downturn due to its larger land bank, which allows BSD more flexibility to tailor its products to customers, including selling large land parcels to co-developers and investors.

CTRA has lower property presales than China-based KWG, but CTRA has stronger domestic market position given its position as one of the largest property developers in Indonesia. We believe the difference in scale is also offset by CTRA's higher non-development interest cover, which underpins its robust financing flexibility. These reasons, combined with the strategic locations of both companies' assets in their respective markets, warrant the same rating level.

Fitch believes CTRA's higher rating relative to Modernland and Alam Sutera is underpinned by CTRA's significantly larger operating presales, supplemented by its healthy non-development interest cover, better geographical diversification in its land bank and projects, and lower leverage.

PT Ciputra Residence (CTRR), which is rated based on the consolidated profile of CTRA, may be compared on the national scale with PT Kawasan Industri Jababeka Tbk (A-(idn)/Stable) and PT PP Properti Tbk (PPRO; BBB+(idn)/Negative). Fitch believes Jababeka's business profile is weaker because CTRR has a significantly larger operating presales scale, more geographically diversified projects and lower business cyclicality due to exposure to residential property sales as opposed to Jababeka's industrial land sales. CTRR also has lower leverage than Jababeka.

Fitch believes CTRR's higher operating presales, wider profit margin, lower leverage and stronger non-development interest cover relative to PPRO, combined with CTRR's better geographic diversification and more established record in residential and commercial property development, warrant a multiple-notch difference between the ratings of the two companies

KEY ASSUMPTIONS

Fitch's Key Assumptions Within Our Rating Case for the Issuer

- Attributable presales of IDR3.7 trillion in 2019 and IDR4.5 trillion in 2020
- Discretionary land acquisition spending of around IDR650 billion in 2019 and around IDR1 trillion in 2020
- Total construction capex of IDR2.5 trillion-4 trillion in 2019-2023

RATING SENSITIVITIES

Developments That May, Individually or Collectively, Lead to a Stable Outlook

- Presales improve in the next two years in line with Fitch's expectations, leading to annual attributable presales of more than IDR5 trillion by 2021

Developments That May, Individually or Collectively, Lead to a Downgrade

- If non-development gross profit/net interest expense remains above 1x, then leverage, as measured by net adjusted debt/ adjusted inventory, sustained above 40%
- Inability to improve attributable presales to more than IDR5 trillion by 2021
- Weakening in overall legal and operational ties between the parent and the operating subsidiaries

LIQUIDITY

Sufficient Liquidity: As of 31 March 2019, CTRA had around IDR3.4 trillion of consolidated cash and over IDR2 trillion of undrawn debt facilities. This compared with around IDR1.3 trillion of short-term debt maturities, of which around IDR1 trillion is a short-term working-capital facility that would be typically rolled over in the normal course of business, given CTRA's established track record and strong market position as a leading property developer in Indonesia.

CTRA's capex in the next 24 months mainly comprises construction costs for its three new

shopping malls and properties for sale. The construction costs for property sales are relatively flexible, as they are partly contingent upon meeting sales thresholds in the current period. In addition, its land acquisitions are discretionary. All these factors may allow the company to accumulate cash and shore up its liquidity profile if required. Liquidity is also supported by CTRA's access to local banks and capital markets

FULL LIST OF RATING ACTIONS

PT Ciputra Development Tbk
- Long-Term Issuer Default Rating affirmed at 'BB-'; Outlook revised to Negative from Stable
- SGD150 million 4.85% senior unsecured bond affirmed at 'BB-'

PT Ciputra Residence
-National Long-Term Rating affirmed at 'A+(idn)'; Outlook revised to Negative from Stable
- Senior unsecured debt class affirmed at 'A+(idn)'
- IDR80 billion bond with partial credit guarantee from the International Finance Corporation affirmed at 'AA-(idn)'

Contact:
Primary Analyst
Bernard Kie (International Rating)
Associate Director
+65 6796 7216
Fitch Ratings Singapore Pte Ltd
One Raffles Quay
South Tower #22-11
Singapore 048583

Guninta Sudiar (National Rating)
Analyst
+62 21 2988 6811
PT Fitch Ratings Indonesia
DBS Bank Tower
Jl Prof Dr Satrio Kav 3-5
Jakarta 12940

Secondary Analyst
Guninta Sudiar

Analyst
+62 21 2988 6811

Committee Chairperson
Hasira De Silva, CFA
Senior Director
+65 6796 7240

Summary of Financial Statement Adjustments:

- CTRA reports land purchase costs under investment cash flows (capex). We have removed these costs from cash flow from investments and included them under cash flow from operations as working capital.
- The company reports land bank as a long-term asset on its balance sheet. We have classified land bank as part of current inventory given the nature of CTRA's business of land development and sales. We have also classified advances from customers as part of working capital.
- We have moved 'final tax' to after the 'profit before income tax' line in the income statement.
- We have proportionately consolidated the key financials of CTRA's major subsidiaries to reflect significant minority interests

Note to editors: Fitch's National ratings provide a relative measure of creditworthiness for rated entities in countries with relatively low international sovereign ratings and where there is demand for such ratings. The best risk within a country is rated 'AAA' and other credits are rated only relative to this risk. National ratings are designed for use mainly by local investors in local markets and are signified by the addition of an identifier for the country concerned, such as 'AAA(idn)' for National ratings in Indonesia. Specific letter grades are not therefore internationally comparable

Media Relations: Peter Hoflich, Singapore, Tel: +65 6796 7229, Email: peter.hoflich@thefitchgroup.com
Leslie Tan, Singapore, Tel: +65 6796 7234, Email: leslie.tan@thefitchgroup.com

Additional information is available on www.fitchratings.com

Applicable Criteria

Corporate Rating Criteria (pub. 19 Feb 2019)
Corporates Notching and Recovery Ratings Criteria (pub. 23 Mar 2018)
Country-Specific Treatment of Recovery Ratings Criteria (pub. 18 Jan 2019)
National Scale Ratings Criteria (pub. 18 Jul 2018)
Parent and Subsidiary Rating Linkage (pub. 16 Jul 2018)

Sector Navigators (pub. 23 Mar 2018)
Third-Party Partial Credit Guarantees Rating Criteria - Effective from 27 June 2018 to 11 June 2019 (pub. 27 Jun 2018)

Additional Disclosures
Dodd-Frank Rating Information Disclosure Form
Solicitation Status
Endorsement Policy