FitchRatings

RATING ACTION COMMENTARY

Fitch Downgrades Ciputra Development to 'B+', Affirms Ciputra Residence at 'A(idn)'; Outlook Stable

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Fitch Ratings - Singapore - 30 Nov 2020: Fitch Ratings has downgraded Indonesian homebuilder PT Ciputra Development Tbk's (CTRA) Long-Term Issuer Default Rating (IDR) to 'B+' from 'BB-'. The Outlook is Stable. Fitch has also downgraded CTRA's SGD150 million 4.85% senior unsecured notes due September 2021 to 'B+' with a Recovery Rating of 'RR4' from 'BB-'. At the same time, PT Fitch Ratings Indonesia has affirmed the National Long-Term Rating of CTRA's subsidiary, PT Ciputra Residence (CTRR), at 'A(idn)' and revised the Outlook to Stable from Negative. A full list of rating actions is at the end of this commentary.

The downgrade of the Long-Term IDR reflects Fitch's view that CTRA's scale is no longer consistent with a 'BB-' rating. We believe CTRA will not be able to increase its attributable pre-sales (including its share in jointly owned subsidiaries) to more than IDR5 trillion by 2022, the timeline we had set to achieve the minimum level for a 'BB-' rating.

We first highlighted the scale risks in 2019 with the belief that CTRA would achieve more than IDR5 trillion in attributable pre-sales in 2020-2021. However, the coronavirus pandemic will delay recovery prospects to beyond 2022, in our view. We expect demand for affordable homes to remain healthy in the next 12-18 months and drive modest pre-sales growth, but we do not expect this alone to be sufficient to raise CTRA's pre-sales above the IDR5 trillion threshold, as demand from investors and upgraders, who typically buy more expensive homes and high-rise units, is likely to remain soft.

The Stable Outlook on the ratings reflects CTRA's sufficient geographical and product diversity that has allowed the company to nimbly shift its pre-sales mix towards landed affordable homes - defined by Fitch as properties priced at or under IDR1.5 billion per unit - for which demand has held up well amid the current downturn, even as sales of high-rise and more expensive homes fell. We expect CTRA to maintain annual attributable pre-sales at more than IDR4 trillion over the medium term.

CTRR's National Long-Term Rating is based on the consolidated financial profile of its stronger parent, CTRA, given the strong linkages between the companies, as defined in Fitch's Parent and Subsidiary Linkage Rating Criteria.

'A' National Ratings denote expectations of a low level of default risk relative to other issuers or obligations in the same country or monetary union.

KEY RATING DRIVERS

Modest Recovery in Pre-Sales: We expect CTRA to post attributable pre-sales of IDR4.3 trillion in 2021 and IDR4.9 trillion in 2022, from around IDR4 trillion forecast for 2020 and IDR4.4 trillion in 2019. However, our forecasts are subject to a high degree of uncertainty related to the path of the pandemic globally and in Indonesia. We believe landed-home sales will account for a large majority in 2020 and 2021 (10M20: 73%; 2017-2019 average: 54%), and we expect CTRA to maintain its focus on homes priced under IDR2 billion per unit targeting end-users rather than investors and upgraders.

Weaker Non-Development Cash Flows: We expect CTRA's non-development gross profit (before depreciation and amortisation) as a ratio to net interest expense to fall to around 1.0x in 2020, from 1.8x in 2019, as the company had to offer significant rebates to shopping mall tenants to combat the effects of social distancing on their sales, in line with market norms.

We expect non-development gross profit interest cover to recover modestly to 1.4x by 2023 due to our belief the health crisis will remain largely unaddressed until after 2021, and international travel - a key driver of CTRA's hotel earnings - will only improve meaningfully in 2022. On the other hand, CTRA's hospitals recovered well in 3Q20 with revenue from coronavirus-related services rising rapidly to offset lower revenue from traditional elective procedures, a trend we expect will continue in the next 12-18 months.

Limited Near-Term Foreign-Ownership Impact: We do not expect Indonesia's relaxation of rules to allow foreigners to own high-rise properties to have a meaningful impact on CTRA's pre-sales in the next one-to-two years, as long as the health crisis remains largely unaddressed and international business travel has not normalised. However, over the longer term, the changes, if the regulations are implemented without ambiguity, may help raise sales for the sector. CTRA has over 200,000 sq m in sellable mixed-development area in Greater Jakarta, which would be attractive to foreign property investors.

Strong Financial Profile: We expect CTRA to maintain homebuilder leverage, defined as net debt/adjusted inventory, of around 30% over the next few years (2020 forecast: 28%; 2019: 27%). We believe its cash flow from operations will remain neutral over the medium term, supported by faster cash collections and more flexible construction costs on landed homes, which will largely cover CTRA's land purchase outlay.

Free cash flow (FCF)/gross debt may weaken to around -9% to -10% in 2020-2021 as CTRA completes investment-property construction, and drop to low-single digits thereafter as we expect the company to slow its capex as it re-assesses demand for commercial properties and hotels in the current environment.

Large Land Bank, Minority Interests: CTRA had around 2,341 hectares in land bank at end-3Q20, with a sizeable presence in the main urban areas of Greater Jakarta and Greater Surabaya. The land bank supports over 15 years of development, a key competitive advantage. The group also develops projects with land owners on a profit- or revenue-sharing basis, expanding its operational scale while limiting the balance-sheet burden. We expect CTRA to provide support to joint ventures based on its shareholding due to the reputational risk. We have proportionately consolidated the key financials of major subsidiaries when computing CTRA's financial metrics.

Parent-Subsidiary Linkage: CTRA and its subsidiaries have strong operational and strategic linkages from common shareholders and board members. CTRR is considered strategically important as it owns most of CTRA's Jakarta land bank, accounting for 23% of 2019 consolidated revenue. CTRA and its subsidiaries have moderate legal linkages from a cross-default provision in CTRA's SGD150 million cross-border unsecured notes. We believe there is reputational risk to CTRA from the subsidiaries' use of the "Ciputra" brand. We therefore treat the group as a single operating entity.

DERIVATION SUMMARY

CTRA's IDR can be compared with that of PT Bumi Serpong Damai Tbk (BSD, BB-/Stable), while CTRR's National Long-Term Rating can be compared with that of PT Kawasan Industri Jababeka Tbk (KIJA, B-/BBB-(idn)/Stable) and PT Buana Lintas Lautan Tbk (BULL, A-(idn)/Negative).

BSD is rated one-notch higher than CTRA to reflect its larger pre-sales scale as we expect BSD to maintain attributable pre-sales of more than IDR5 trillion over the medium term, notwithstanding the current economic downturn, compared with IDR4 trillion-5 trillion for CTRA. BSD also has a significantly larger land bank than CTRA, and higher EBITDA margins of around 45% over the next few years, which supports stronger CFFO generation, compared with around 30% EBITDA margins for CTRA. BSD also has a larger portfolio of non-development EBITDA-generating shopping malls, offices and hotels, which we expect will cover its interest costs by an average 1.2x over the next four years, compared with around 0.9x for CTRA, which provides BSD with more financial flexibility during economic downturns.

KIJA's IDR and National Long-Term Rating are multiple notches below CTRA's IDR and CTRR's National Long-Term Rating to reflect its smaller operating scale as we expect attributable pre-sales to hover under IDR1 trillion in the next two years. Around half of KIJA's pre-sales stem from the sale of industrial land, which is more volatile during economic downturns, and the company's pre-sales are concentrated in its two main townships, compared with CTRR's significantly greater geographical and product diversity. CTRR's financial profile is also stronger than that of KIJA as we expect leverage to hover around 30% in the next few years, compared with around 50% for KIJA.

BULL's National Long-Term Rating of 'A-(idn)' with a Negative Outlook is lower than CTRR's rating to reflect its increased cash-flow volatility on account of a rising mix of spot-rate charter revenue on the back of its recent aggressive fleet expansion. We also believe CTRA has a stronger liquidity position, with cash on hand net of next 12 months' FCF sufficient to cover next 12 months' debt maturities, whereas BULL may have to rely on lenders rolling over some of its current term-loan maturities, which is subject to the value of its fleet remaining steady and providing sufficient collateral cover.

KEY ASSUMPTIONS

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

- Attributable pre-sales of IDR4.3 trillion in 2021 and IDR4.9 trillion in 2022

- Annual land banking expenses of around IDR400 billion-600 billion from 2020-2024

- Capex of around IDR500 billion in 2020, reducing to less than IDR200 billion in 2021

Key Recovery Rating Assumptions

- The recovery analysis assumes CTRA will be liquidated in a bankruptcy rather than continue as a going concern because it is an asset-trading company

- To estimate liquidation value, we assume a 75% advance rate against the value of accounts receivable and a 50% advance rate against inventory, investment properties and other plant, property and equipment. We believe the company's reported land-bank value, which is based on historical land cost, is at a significant discount to current market value - as reflected in gross profit margins of around 50% on average on property sales, and, thus, is already conservative.

- We assume that CTRA's approximately IDR8 trillion in secured bank loans outstanding as of 30 September 2020 will rank prior to its SGD150 million senior unsecured notes in a liquidation

- We have deducted 10% of the resulting liquidation value for administrative claims

- The above estimates result in a recovery rate corresponding to an 'RR1' Recovery Rating for CTRA's senior unsecured notes. Nevertheless, we have rated the senior notes at 'B+' with a Recovery Rating of 'RR4' because, under Fitch's Country-Specific Treatment of Recovery Ratings Rating Criteria, Indonesia falls into 'Group D' of creditor friendliness. Instrument ratings of issuers with assets in this group are subject to a soft cap at the issuer's IDR.

RATING SENSITIVITIES

Factors that could, individually or collectively, lead to positive rating action/upgrade:

- Annual attributable pre-sales sustained above IDR5 trillion

Factors that could, individually or collectively, lead to negative rating action/downgrade:

- Annual attributable pre-sales sustained below IDR3.5 trillion

- Net debt/adjusted inventory sustained above 45%, as long as non-development gross profit excluding depreciation and amortisation/net interest cover is sustained at or above 1.0x

- Weakening in overall legal and operational ties between the parent and the operating subsidiaries

BEST/WORST CASE RATING SCENARIO

International scale credit ratings of Non-Financial Corporate issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of four notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit https://www.fitchratings.com/site/re/10111579.

LIQUIDITY AND DEBT STRUCTURE

Comfortable Liquidity: CTRA had IDR4.4 trillion in cash on hand as of 30 September 2020, which, net of Fitch's estimate of an aggregate FCF deficit of around IDR1 trillion starting 4Q20 through to end-2021, is sufficient to cover maturing term loans and bonds of around IDR3 trillion. The company has a record of maintaining more diversified fund sources compared with domestic peers, with a ratio of cross-border debt to domestic bank debt of 20:80 as of 30 September 2020. This mitigates refinancing risk, in Fitch's view, in the event cross-border debt markets tighten. The company has minority shareholders in several key subsidiaries, but Fitch estimates that more than 90% of CTRA's cash and equivalents are in wholly owned subsidiaries, which therefore supports sufficient cash fungibility.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG CONSIDERATIONS

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg

RATING ACTIONS

ENTITY/DEBT	RATING			RECOVERY	PRIOR
PT Ciputra Residence	Natl LT	A(idn) Rating Outlook Stable	Affirmed		A(idn) Rating Outlook Negative
• senior unsecured	Natl LT	A(idn)	Affirmed		A(idn)
• senior unsecured	Natl LT	A+(idn)	Affirmed		A+(idn)
PT Ciputra Development Tbk	LT IDR	B+ Rating Outlook Stable	Downgrade		BB- Rating Outlook Negative
• senior unsecured	LT	B+	Downgrade	RR4	BB-

VIEW ADDITIONAL RATING DETAILS

FITCH RATINGS ANALYSTS

Salman Alamsyah
Associate Director
Primary Rating Analyst
National

+62 21 2988 6818
PT Fitch Ratings Indonesia
DBS Bank Tower 24th Floor, Suite 2403 Jl. Prof.Dr. Satrio Kav 3-5 Jakarta 12940

Hasira De Silva, CFA
Senior Director
Primary Rating Analyst
International
+65 6796 7240
Fitch Ratings Singapore Pte Ltd.
One Raffles Quay #22-11, South Tower Singapore 048583

Salman Alamsyah
Associate Director
Secondary Rating Analyst
International
+62 21 2988 6818

Vicky Melbourne
Senior Director
Committee Chairperson
+61 2 8256 0325

MEDIA CONTACTS

Alanis Ko
Hong Kong
+852 2263 9953
alanis.ko@thefitchgroup.com

Leslie Tan
Singapore
+65 6796 7234
leslie.tan@thefitchgroup.com

Peter Hoflich
Singapore
+65 6796 7229
peter.hoflich@thefitchgroup.com

Additional information is available on www.fitchratings.com

APPLICABLE CRITERIA

Corporates Notching and Recovery Ratings Criteria (pub. 14 Oct 2019) (including rating assumption sensitivity)

Country-Specific Treatment of Recovery Ratings Rating Criteria (pub. 27 Feb 2020)

Corporate Rating Criteria (pub. 01 May 2020) (including rating assumption sensitivity)

National Scale Rating Criteria (pub. 08 Jun 2020)

Third-Party Partial Credit Guarantees Rating Criteria (pub. 22 Jun 2020)

Sector Navigators - Addendum to the Corporate Rating Criteria (pub. 26 Jun 2020)

Parent and Subsidiary Linkage Rating Criteria (pub. 26 Aug 2020)

APPLICABLE MODELS

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

Corporate Monitoring & Forecasting Model (COMFORT Model), v7.9.0 (1)

ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

Solicitation Status

Endorsement Policy

ENDORSEMENT STATUS

PT Ciputra Development Tbk	EU Endorsed
PT Ciputra Residence	-

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