FitchRatings

Fitch Assigns Lippo Malls Indonesia Retail Trust 'BB' Final Rating

Fitch Ratings - Singapore - 21 October 2019:

Fitch has assigned Lippo Malls Indonesia Retail Trust (LMIRT) a final Long-Term Foreign-Currency Issuer Default Rating (IDR) of 'BB' with Stable Outlook, and a final rating of 'BB' to its USD250 million 7.25% senior unsecured notes due in 2024. The bonds are issued by LMIRT's wholly owned subsidiary, LMIRT Capital Pte. Ltd., and guaranteed by Perpetual (Asia) Limited in its capacity as the trustee of LMIRT.

The final IDR follow LMIRT's announcement that the company and PT Lippo Karawaci Tbk (Lippo, B-/Stable) have agreed to extend the deadline for the completion of the segregation process and the long stop date to complete the Lippo Mall Puri acquisition to 31 March 2020 and 30 June 2020, from the previous plan to complete them in 2H19. The expected IDR assigned to LMIRT on 3 June 2019 was based on the assumption that LMIRT will complete the acquisition in 2H19 and maintain a loan-to-value (LTV) ratio (net debt/investment property value) of around 35% after the acquisition.

The delay in completing the Lippo Mall Puri acquisition does not impact LMIRT's rating. We believe that Lippo Mall Puri does not materially change LMIRT business risk profile, while LMIRT's financial profile, characterised by FFO fixed-charge coverage of around 2x and LTV ratio of around 35%, is consistent with its rating. In any case, Fitch had assumed that that the acquisition of Lippo Mall Puri would be funded using a combination of debt and equity such that LMIRT maintains an LTV ratio of 35%.

The final ratings on the USD250 million senior unsecured notes follows the receipt of final documents conforming to information already received and is the same as the expected rating assigned on 3 June 2019.

Key Rating Drivers

Largest Indonesian Shopping-Mall Portfolio: LMIRT's shopping-mall portfolio is the largest in Indonesia with net lettable area (NLA) of 910,749 square meters, more than 3,697 tenants and estimated annual shopper traffic of 169.8 million as of 31 December 2018. Fitch expects the portfolio's average occupancy rate to hover around 91%-92% over the next two years, which is above the current industry average of 81%-83%. The above-average occupancy reflects LMIRT's well-located assets and favourable demand-supply dynamics in most of its catchment areas.

LMIRT's lease expiry profile is manageable with 4.9% of NLA expiring from 30 September 2019 to 31 December 2019 and 18.9% in 2020. In addition, leases that are not coming up for renewal have built-in annual rental increases and Fitch expects the performance of several of LMIRT's under-utilised shopping malls to improve. These factors support Fitch's forecast of modest EBITDA growth over the medium term.

Ring-Fenced from Lippo: Fitch rates LMIRT on a standalone basis because we believe the trust is sufficiently ring-fenced from Lippo, which owns 31.57% of LMIRT's equity and controls the trust's manager. LMIRT has right of first refusal over Lippo's shopping malls, and a large portion of its malls were purchased from its sponsor. However, LMIRT, as a REIT listed in Singapore, is subject to stringent regulations that require two independent valuations and minority unitholders' approval for related-party transactions. Fitch believes these rules sufficiently mitigate the risks that such transactions are detrimental to minority unitholders.

Manageable Related-Party Tenant Risk: As of end-June 2019, around 25% of LMIRT's gross revenue was to related-party tenants, including 8% from master leases with LPKR on three of its malls, and around 4% from unprofitable supermarket operator PT Matahari Putra Prima Tbk (Hypermart). We expect revenue from master-leased malls to fall significantly at contract expiry, given the underlying tenant revenue and occupancy are considerably lower than the contracted values. The master lease for Lippo Mall Kemang, the largest of the three, expires on 16 December 2019 and we have assumed revenue from the mall will fall by around 30%, which we estimate will drag down LMIRT's total revenue by around 4%.

Hypermart remains current on its rental payments to LMIRT, but it reduced its space by 7.7% so far this year, with a 10% reduction planned for 2019, as part of its business rationalisation. We have assumed that LMIRT will be able to fill about 50% of the total space vacated by Hypermart in the first year, but expect the replacement tenants to pay a higher rent per square foot than Hypermart, in line with the trend of the last 12 months. Accordingly, the cash flow impact from Hypermart's space reduction will be broadly neutral.

Mall Puri Purchase Pending: LMIRT signed a conditional sales and purchase agreement with LPKR in March 2019 to purchase Lippo Mall Puri for around SGD350 million. Puri is a relatively new mall, and is part of the St. Moritz mixed-development in West Jakarta, which should support an increase in tenant demand over the medium term.

Puri's occupancy stood at 91.6% as of end-June 2019, which is in line with trust's average of around 92%. The sponsor has committed to provide annual rental support payments to LMIRT during the first five fiscal years after the purchase of the mall. The purchase price does not factor in this rental support income. The sponsor expects to pre-fund the rental support payments as well as its 31.57% share of the new equity that LMIRT plans to issue via a USD730 million rights issue that is targeted to be completed in 1Q20. We expect that LMIRT will fund the purchase using a combination of debt and equity in order to maintain LTV of around 35%.

Perpetual Securities Treated as Equity: Fitch treats LMIRT's SGD260 million of perpetual securities - issued in 2016 and 2017 - as 100% equity, as these securities have strong going-concern and gone-concern loss-absorption features. Our treatment also factors in LMIRT's intention to maintain these securities as a permanent part of its capital structure, by replacing the securities at their next call-dates with similar instruments or common equity.

Derivation Summary

LMIRT's Long-Term IDR can be compared to PT Pakuwon Jati Tbk (BB/Stable) and Emirates REIT (BB/Stable).

Pakuwon is a Indonesia-based property developer whose rating is driven by its large investment property portfolio consisting of primarily shopping malls, with some office and hotel assets. For similar assets, Fitch views that Pakuwon's investment properties are of better quality than those of LMIRT, indicated by stronger occupancy and rent per square foot. This coupled with Pakuwon's conservative capital structure leads to an overall stronger financial profile than LMIRT. However, Pakuwon has higher exposure to the more-risky property development business, while the robust regulatory frameworks for Singapore-listed REITs compensate for LMIRT's weaker financial profile than Pakuwon. As a result, Fitch rates both companies at the same level.

Emirates REIT is based in the United Arab Emirates. It has a resilient portfolio of office and school properties in Dubai. Emirates REIT has a higher leverage and lower portfolio occupancy than LMIRT, however, these are offset by its strong asset quality, better earnings visibility via longer lease durations of its school assets, and beneficial government relations. These support Emirates REIT's ratings at the same level as those of LMIRT.

Key Assumptions

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

- Broadly stable occupancy rates at around 90% and modest rental rate growth of around 3.5% a year to 2020. Revenue decline in Kemang is compensated by improvements in weaker assets from asset enhancement initiatives, while stronger assets continue to exhibit stable performance and rental rate growth.

- US dollar bonds issued to refinance SGD175 million term loans due in 2020 and SGD120 million short-term working capital facility.

- Master lease at Lippo Mall Kemang, Kuta, and Yogyakarta will expire in December 2019, 2021, and 2022 - and will not be extended.

RATING SENSITIVITIES

Developments That May, Individually or Collectively, Lead to Positive Rating Action

- Fitch does not expect any positive rating action over the medium term given LMIRT's operating scale

Developments That May, Individually or Collectively, Lead to Negative Rating Action

- Net debt / investment property of above 35% on a sustained basis

- FFO fixed-charge cover ratio of below 1.5x on a sustained basis

- A sustained weakening in the performance of LMIRT's shopping mall portfolio as indicated by falling occupancy rates and negative rental reversion

Liquidity and Debt Structure

Adequate Liquidity, Financial Flexibility: LMIRT has refinanced the SGD120 million revolving credit facility due in 2019 and the SGD175 million term loan due in 2020 using proceeds from the US dollar notes. The trust maintains the SGD120 million revolver as an undrawn liquidity line following the bond issuance. The next significant maturity is SGD75 million of bonds due in June 2020. LMIRT will have a cash balance of around SGD93 million at end-2019 by Fitch's estimates, but it also has undrawn uncommitted credit lines of SGD120 million to cover this maturity.

LMIRT, as with most REITs, is exposed to refinancing risk because it is required to pay out at least 90% of its distributable profits to unitholders. However we expect the trust to be able to meet its refinancing needs due to its adequate financial profile, unencumbered property portfolio, and comfortable LTV of around 35% over the medium term.

ESG Considerations

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of 3 - 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 our ESG Relevance Scores, visit www.fitchratings.com/esg

RATING ACTIONS

ENTITY/DEBT	RATING		PRIOR
LMIRT Capital Pte. Ltd.			
senior unsecured	LT BB New Rating		BB(EXP)
Lippo Malls Indonesia Retail Trust	LT IDR BB New Rating		BB(EXP)

Additional information is available on www.fitchratings.com

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Applicable Criteria

Sector Navigators (pub. 23 Mar 2018)
Corporate Hybrids Treatment and Notching Criteria (pub. 09 Nov 2018)
Country-Specific Treatment of Recovery Ratings Criteria (pub. 18 Jan 2019)
Corporate Rating Criteria (pub. 19 Feb 2019)
Parent and Subsidiary Rating Linkage (pub. 27 Sep 2019)
Corporates Notching and Recovery Ratings Criteria (pub. 14 Oct 2019)

Additional Disclosures

Dodd-Frank Rating Information Disclosure Form
Solicitation Status
Endorsement Policy

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