FitchRatings

Fitch Assigns First-Time 'B(EXP)' Rating to Intiland; Rates USD Bonds 'B(EXP)'

Fitch Ratings-Singapore-27 July 2018: Fitch Ratings has assigned Indonesia-based property developer PT Intiland Development Tbk's an expected Long-Term Foreign-Currency Issuer Default Rating (IDR) of 'B(EXP)' with a Stable Outlook. At the same time, the agency has assigned the company an expected senior unsecured rating of 'B(EXP)' and an expected rating of 'B(EXP)' on its proposed US dollar senior unsecured notes with a Recovery Rating of 'RR4', to be issued by Intiland and guaranteed by certain subsidiaries.

The expected IDR assumes that Intiland will raise sufficient funds from the proposed US dollar notes to refinance secured debt, which will improve the company's liquidity and capital structure. The final ratings are contingent on the successful issue of the proposed bond.

The ratings reflect Intiland's long property development record in Jakarta and Surabaya - Indonesia's two largest cities. The company's residential projects are mostly located within proximity of each city's central business district and therefore target more affluent middle- to high-end buyers. The ratings are constrained by limited leverage headroom, as measured by net debt/adjusted inventory, and more volatile presales than 'B' category peers. Fitch believes the company's ability to raise new borrowings will be constrained under the proposed note issuance, at least until 2021, as fixed-charge cover, as defined in the documentation, will be below the minimum 2.5x. However, the documentation allows for permitted indebtedness, which we believe will be sufficient to finance construction.

KEY RATING DRIVERS

Recovering Attributable Presales: Fitch expects Intiland to book annual attributable presales of around IDR2 trillion over the medium-term, a level broadly in line with 'B' category peers. The company's key target market of middle- to high-end buyers increases presale volatility above that of peers in the mass-market segment, as its target market is more sensitive to macroeconomic and political adversity. This risk is mitigated to some extent by Intiland's geographically dispersed projects, which increase product flexibility. Fitch also expects Intiland's mix of completed but unsold inventories, which are more appealing for end-buyers than newer projects, to contribute to presales in the short term.

Intiland's attributable presales stood at IDR527 billion in 1H18. This lagged Fitch's full-year estimate of IDR1.7 trillion due to weaker-than-Fitch-expected industrial land sales and the combination of a May 2018 terror attack in Surabaya, long Idul Fitri holiday and soft demand temporarily affecting sales and launch schedules. This situation has normalised and the company expects pre sales to ramp up in 2H18 as it proceeds with new-project launch schedules in September and October 2018.

High Leverage Limits Rating Headroom: Fitch expects Intiland's leverage, as measured by net debt/adjusted inventory, to remain elevated at around 45%, and therefore to limit its rating headroom. This is because Intiland may need to replenish landbank, particularly for its high-rise projects within the central business district, which commands higher acquisition costs. This is in contrast to peers' ability to deleverage quickly from large and low-cost landbank inventory.

Adjustments for Joint-Venture Cash Flow: A joint venture with Singapore's sovereign wealth fund, GIC - which has invested in Intiland's 57 Promenade and South Quarter Jakarta projects - has helped the company accelerate development and deleverage. Of IDR980 billion cash received for both projects, IDR844 billion has been used to repay project-related loans, reducing Intiland's consolidated leverage, as measured by net debt/adjusted inventory, to 37% in 2017, from 54% in 2016. However, Fitch understands cash flow from both projects is ringfenced, meaning Intiland may have limited cash flow access.

Fitch factors in minority interests in these projects by using proportionate presales when calculating inventory turnover, as measured by presales/gross debt, and deconsolidates both projects in the leverage ratio, as measured by net debt/adjusted inventory. Both projects have low leverage, and therefore, after the adjustments, the ratios stood at 50% and 42%, respectively, as of end-2017.

Low Margin to Improve: Fitch expects Intiland's low margin to improve over the next few years, as the company recognises profit from higher-margin projects, such as South Quarter, 57 Promenade and Graha Golf. The company's low margin compared with that of other Fitch-rated Indonesian developers stems from its high-rise residential development focus and the discounts it has offered over the previous two years to reduce inventory holdings. Key projects launched in the previous few years, including Serenia Hills and 1 Park Residences, were also recently acquired, increasing its land acquisition costs compared with township peers that benefit from a large, low-cost landbank.

Manageable Development Risk: Intiland has manageable development risk, despite a large proportion of high-rise, niche-market projects, due to limited capex commitments that allow it to better manage cash flow. Management's strategy to start construction only when a minimum presales target is achieved, historically around 60%, effectively covers construction costs. Development risks are also somewhat counterbalanced by Intiland's landed township project in Surabaya, where it has an established record in the upscale residential segment, and its large, mature industrial estate in Ngoro, near Surabaya, from which it has generated consistent annual presales for the previous four years.

Expanding Investment Portfolio: Fitch estimates that Intiland's attributable non-development income increased to IDR500 billion in 2017, from around IDR200 billion in 2015, and expects it to continue rising over the long-term, supported by improving occupancy and two additional hotels under construction in Praxis and Spazio Tower. Non-development gross profit/net interest cover should move closer to 1.0x by end-2022, from 0.4x at end-2017. The company has an expanding investment portfolio, primarily the South Quarter office tower that opened in mid-2016 and has a 71% occupancy rate and a weighted-average lease maturity of over seven years.

DERIVATION SUMMARY

Intiland's risk profile is comparable with that of PT Alam Sutera Realty Tbk (ASRI, B/Stable) and PT Modernland Realty Tbk (B/Stable). ASRI's higher presales, which Fitch forecasts at IDR3 trillion in 2018, and better margin from its large, low-cost landbank are counterbalanced by higher leverage, which Fitch forecasts at 52.3% for 2018, and a lower non-development income contribution. Fitch expects Intiland and Modernland to generate a similar amount of annual attributable presales, at around IDR2 trillion, over the medium-term, and believes Intiland's lower development margin is compensated by a stronger recurring profile over the medium-term.

KEY ASSUMPTIONS

Fitch's Key Assumptions Within Our Rating Case for the Issuer
- Attributable presales of IDR1.7 trillion in 2018 and IDR2.5 trillion in 2019
- Majority of bond proceeds used to refinance debt
- Minimal capex in 2018 and IDR260 billion in 2019

Key Recovery Rating Assumptions:
- Recovery analysis assumes Intiland would be liquidated in a bankruptcy rather than continue as a going concern because it is an asset-heavy company. The analysis is based on management accounts as of 30 June 2018.
- 75% recovery from accounts receivable
- 75% recovery from inventory
- 50% recovery from development landbank
- 50% recovery from investment properties and fixed assets
- Fitch estimates Intiland's liquidation value will cover 100% of its secured debt and 82% of its unsecured debt, corresponding to a 'RR2' Recovery Rating for the senior unsecured notes after adjusting for administrative claims. The Recovery Rating is, however, capped at 'RR4', because under Fitch's Country-Specific Treatment of Recovery Ratings 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

Fitch does not expect positive rating action over the next 18 to 24 months due to Intiland's high business-risk profile and high leverage stemming from its lack of land replenishment compared with 'B' rated peers.

Developments that may, individually or collectively, lead to negative rating action include:
- Attributable presales/gross debt at less than 45% (2017: 50%)
- Leverage, as measured by net debt/adjusted inventory, based on deconsolidated numbers, at more than 50% (2017: 42%)

LIQUIDITY

Proposed Bonds Improve Flexibility: Fitch expects Intiland's financial flexibility and liquidity profile to substantially improve upon the successful issuance of its proposed bonds. This is because the bond proceeds will partially refinance secured, amortising term loans and improve the company's cash flow flexibility in light of its volatile presales and high cash flow commitments for high-rise projects.

The company had IDR528 billion of unrestricted cash at end-2017, against the current portion of long-term debt of IDR954 billion. Fitch believes Intiland has adequate access to bank funding, as seen from its relationships with multiple local and regional banks and record of domestic bonds issuance. The company also has around IDR925 billion of undrawn bank lines to support near-term liquidity if required.

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Summary of Financial Statement Adjustments:
- Fitch adjusts presales from 57 Promenade and South Quarter, and non-development income from South Quarter, to reflect only Intiland's effective ownership- Fitch deconsolidates 57 Promenade and South Quarter and adds back Intiland's equity shares when computing the net debt/adjusted inventory ratio
- Fitch reclassifies long-term inventory and advances from customers as part of working capital

For regulatory purposes in various jurisdictions, the supervisory analyst named above is deemed to be the primary analyst for this issuer; the principal analyst is deemed to be the secondary.

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Applicable Criteria

Corporate Rating Criteria (pub. 23 Mar 2018) (https://www.fitchratings.com/site/re/10023785)
Corporates Notching and Recovery Ratings Criteria (pub. 23 Mar 2018) (https://www.fitchratings.com/site/re/10024585)
Sector Navigators (pub. 23 Mar 2018) (https://www.fitchratings.com/site/re/10023790)

Additional Disclosures

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