

14 October 2020

Consumer Cyclical | Leisure & Entertainment

## The Erawan Group (ERW TB)

**Sell** (Maintained)

**Still Heavily Dependent On Local Market; SELL**

Target Price (Return): THB2.50 (-13.2%)  
 Price: THB2.88  
 Market Cap: USD233m  
 Avg Daily Turnover (THB/USD) 55.4m/1.77m

- **Keep SELL and THB2.50 TP (DCF), 13% downside.** We expect The Erawan Group to record a THB426m net loss in 3Q20F. Negative earnings may continue into 1H21F, in the absence of a material recovery in the international tourism market, price competition, and rising fixed costs.
- **Pent-up demand for leisure traveling among locals** should improve the performance of Erawan's hotels in Pattaya and Hua Hin – a short-driving distance from Bangkok – which resumed operations in July, to achieve up to 80% occupancy rates (OR) during weekends and 20% on weekdays. However, as its major properties in Bangkok may still record c.20% OR, we expect the average OR for its non-Hop Inn budget hotels to remain at 13% in 3Q20F, resulting in a -90% YoY revenue per available rooms (RevPar) for the quarter.
- **Resilient Hop Inns.** Its Hop Inn budget hotels in Thailand seem to be the strongest segment, given its focus on local business and leisure travellers – with both activities almost at normal levels. The strong demand should enhance its room pricing ability. We expect a 67% 3Q20F OR (3Q19: 71%, 2Q20: 23%), and RevPar decline of 4% YoY. We should see a recovery to pre-pandemic levels in 4Q20F. The segment's contribution should rise to 18%-14% in 2020-2021 vs 2019's 8%. However, its Philippines Hop Inn operations could take another year to recover, due to COVID-19. Overseas OR may remain at c.20%, with -70% YoY RevPar in 3Q20F.
- **3Q20F preview:** We expect Erawan to post a THB426m net loss in Q3 vs THB43m net profit in 3Q19, and 32% better than the previous quarter's THB625m net loss. Group revenue should improve to THB396m from Q2's THB56m. Despite the resumption of its fixed costs related to re-opening of hotels, we expect its total expenses to decline 43% YoY. As the average OR may still be below the break-even level for EBITDA of 25-30%, we assume -32% GPM, and -78%, -20% EBIT and EBITDA margins.
- **Rising competition, minimal benefits from state quarantine.** While Thailand's borders have just reopened – with restrictions – we expect local hoteliers will still have to depend on the domestic market, at least in 4Q20F-1H21F. We are concerned that the pricing strategies of upper-scale hotels, mainly in Bangkok, and distant resorts, ie Phuket, Chiang Mai, Koh Samui, may affect Erawan's competitiveness in the mid-scale and economy segments. We also expect Erawan to earn a minimal c.TH60-80m/quarter from the extended tourism stimulus measures, from end-Oct to end-Jan 2021. There are 88 Bangkok hotels with 11,360 rooms in the alternative state quarantine (ASQ) program so far, and Erawan has one mid-scale property in the scheme. As tourist arrivals are still capped at c.1,200/month, we do not expect material earnings upside from the ASQ, given the strong supply in the market.
- **Still SELL.** Erawan should gradually see better OR and RevPar. Nonetheless, as we believe a material recovery of international tourism is unlikely throughout 2H20F-1H21F, we expect Erawan's earnings to remain in the red over 4Q20F-2Q21F.

### Analyst

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### Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	(51.6)	(7.7)	(15.3)	(0.7)	(49.9)
Relative	(32.2)	(7.2)	(9.6)	(4.4)	(28.2)
52-wk Price low/high (THB)	1.96 – 6.50				

The Erawan Group (ERW TB)



Source: Bloomberg

Forecasts and Valuation	Dec-18	Dec-19	Dec-20F	Dec-21F	Dec-22F
Total turnover (THBm)	6,280	6,379	2,483	4,425	6,072
Recurring net profit (THBm)	536	463	(1,456)	(230)	185
Recurring net profit growth (%)	7.1	(13.6)	(414.4)	(84.2)	-
Recurring EPS (THB)	0.21	0.18	(0.58)	(0.09)	0.07
DPS (THB)	0.09	0.07	-	-	0.03
Recurring P/E (x)	13.45	15.62	na	na	39.18
P/B (x)	1.27	1.22	1.61	1.70	1.62
Dividend Yield (%)	3.1	2.4	na	na	1.0
Return on average equity (%)	9.8	7.7	(27.9)	(5.2)	4.2
Net debt to equity (%)	149.8	154.8	225.4	265.4	259.1

Source: Company data, RHB

### Note:

Small cap stocks are defined as companies with a market capitalisation of less than USD1bn.

## Financial Exhibits

Asia	Financial summary (THB)	Dec-18	Dec-19	Dec-20F	Dec-21F	Dec-22F
Thailand	Recurring EPS	0.21	0.18	(0.58)	(0.09)	0.07
Consumer Cyclical	EPS	0.21	0.18	(0.58)	(0.09)	0.07
<b>Erawan</b>	DPS	0.09	0.07	-	-	0.03
ERW TB	BVPS	2.26	2.35	1.79	1.70	1.77
Sell	Return on average equity (%)	9.8	7.7	(27.9)	(5.2)	4.2
	Return on average assets (%)	3.3	2.6	(8.0)	(1.2)	1.0
<b>Valuation basis</b>						
DCF.	<b>Valuation metrics</b>	<b>Dec-18</b>	<b>Dec-19</b>	<b>Dec-20F</b>	<b>Dec-21F</b>	<b>Dec-22F</b>
	Recurring P/E (x)	13.45	15.62	na	na	39.18
	P/B (x)	1.3	1.2	1.6	1.7	1.6
	Dividend Yield (%)	3.1	2.4	-	-	1.0
	EV/EBITDA (x)	8.36	8.66	na	14.92	10.32
<b>Key drivers</b>	<b>Income statement (THBm)</b>	<b>Dec-18</b>	<b>Dec-19</b>	<b>Dec-20F</b>	<b>Dec-21F</b>	<b>Dec-22F</b>
i. A recovery of the tourism industry post COVID-19;	Total turnover	6,280	6,379	2,483	4,425	6,072
ii. Opening of new hotels;	Gross profit	2,669	2,650	24	1,330	2,235
iii. Economies of scale in operations, leading to a rise in profit margins.	EBITDA	1,893	1,906	(11)	1,263	1,842
	Depreciation and amortisation	(776)	(830)	(995)	(1,006)	(1,055)
	Operating profit	1,118	1,077	(1,006)	257	787
	Net interest	(360)	(402)	(524)	(519)	(552)
	Pre-tax profit	757	657	(1,530)	(261)	235
	Taxation	(164)	(155)	13	13	(35)
	Reported net profit	536	446	(1,456)	(230)	185
	Recurring net profit	536	463	(1,456)	(230)	185
<b>Key risks</b>	<b>Cash flow (THBm)</b>	<b>Dec-18</b>	<b>Dec-19</b>	<b>Dec-20F</b>	<b>Dec-21F</b>	<b>Dec-22F</b>
i. Weaker-than-expected tourism environment and consumption;	Change in working capital	(86)	49	125	(109)	19
ii. Delays in the opening of new hotel properties;	Cash flow from operations	1,767	1,808	(394)	734	1,216
iii. Rising competition and price pressure in specific hotel segments and locations;	Capex	(1,700)	(1,800)	(1,000)	(1,800)	(1,400)
iv. Unexpected incidents in Thailand and abroad eg. natural disasters, political unrest, etc.	Cash flow from investing activities	(1,727)	(1,841)	(1,000)	(1,800)	(1,400)
	Dividends paid	(225)	(226)	(176)	0	0
	Cash flow from financing activities	(66)	(50)	2,271	694	(46)
	Cash at beginning of period	1,077	1,051	969	1,847	1,474
	Net change in cash	(26)	(82)	878	(373)	(230)
	Ending balance cash	1,051	969	1,847	1,474	1,244
<b>Company Profile</b>	<b>Balance sheet (THBm)</b>	<b>Dec-18</b>	<b>Dec-19</b>	<b>Dec-20F</b>	<b>Dec-21F</b>	<b>Dec-22F</b>
Erawan invests and develops hotel properties that are strategically located to match travellers' varied demands. It owns 65 hotels with 7,883 keys nationwide and five hotels with 843 keys in the Philippines, as of end-2019. Key properties include the Grand Hyatt Erawan Bangkok, JW Marriott Bangkok and Holiday Inn Pattaya, as well as a chain of Ibis and its own Hop Inn budget hotels.	Total cash and equivalents	1,051	969	1,847	1,474	1,244
	Tangible fixed assets	14,975	15,927	15,944	16,748	17,099
	Intangible assets	39	42	29	21	14
	Total investments	93	80	80	80	80
	Total other assets	281	328	328	328	328
	Total assets	16,949	17,834	18,613	19,129	19,328
	Short-term debt	2,274	2,038	3,117	4,619	4,867
	Total long-term debt	7,331	8,126	9,126	8,326	8,026
	Total liabilities	11,240	11,893	14,000	14,806	14,833
	Shareholders' equity	5,667	5,927	4,507	4,277	4,462
	Minority interests	165	179	271	210	197
	Total equity	5,708	5,941	4,613	4,323	4,495
	Total liabilities & equity	16,949	17,834	18,613	19,129	19,328
	<b>Key metrics</b>	<b>Dec-18</b>	<b>Dec-19</b>	<b>Dec-20F</b>	<b>Dec-21F</b>	<b>Dec-22F</b>
	Revenue growth (%)	4.7	1.6	(61.1)	78.2	37.2
	Recurring net profit growth (%)	7.1	(13.6)	(414.4)	(84.2)	0.0
	Recurrent EPS growth (%)	6.9	(13.9)	(413.8)	(84.2)	0.0
	Gross margin (%)	42.5	41.5	1.0	30.1	36.8
	Recurring net profit margin (%)	8.5	7.3	(58.6)	(5.2)	3.0
	Dividend payout ratio (%)	42.0	50.7	(12.1)	0.0	0.0

Source: Company data, RHB

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Figure 1: Erawan's DCF valuation

THBm	2020F	2021F	2022F	2023F	2024F	2025F	2026F	2027F	2028F	2029F
<b>EBIT (1-t)</b>	<b>(920)</b>	<b>302</b>	<b>701</b>	<b>750</b>	<b>841</b>	<b>900</b>	<b>921</b>	<b>941</b>	<b>954</b>	<b>965</b>
Depreciation & amortisation	995	1,006	1,055	1,091	1,091	1,102	1,111	1,123	1,141	1,166
Change in net working capital	125	(109)	19	16	2	4	1	1	(1)	1
Capex	(1,000)	(1,800)	(1,400)	(1,000)	(400)	(400)	(400)	(500)	(600)	(800)
<b>Net free cash flow to firm</b>	<b>(800)</b>	<b>(602)</b>	<b>375</b>	<b>857</b>	<b>1,534</b>	<b>1,605</b>	<b>1,634</b>	<b>1,565</b>	<b>1,495</b>	<b>1,332</b>
Terminal value										23,827
PV	(743)	(519)	300	637	1,059	1,028	972	865	767	11,980
Terminal growth	2.0%									
WACC	7.7%									
Total discounted firm value	16,346									
Less: Net debt	9,757									
Less: Minority interest	271									
Equity value	6,318									
Number of shares (m)	2,518									
<b>Equity value per share (THB)</b>	<b>2.50</b>									

Source: RHB

Figure 2: Operating performance and assumptions

Total Group	2018	2019	2020F	2021F	2022F
Number of rooms	8,485	9,569	10,047	11,288	11,777
Occupancy rate	78%	77%	42%	59%	70%
ARR (THB)	1,837	1,726	1,152	1,281	1,429
% growth	-2%	-6%	-33%	11%	12%
RevPar (THB)	1,440	1,325	481	759	995
% growth	-4%	-8%	-64%	58%	31%
<b>Thailand hotels (excluding Hop Inn)</b>	<b>2018</b>	<b>2019</b>	<b>2020F</b>	<b>2021F</b>	<b>2022F</b>
Number of rooms	4,832	5,343	5,343	5,343	5,343
Occupancy rate	81%	78%	32%	54%	68%
ARR (THB)	2,672	2,570	1,968	2,077	2,272
% growth	5%	-4%	-23%	6%	9%
RevPar (THB)	2,158	2,009	622	1,120	1,556
% growth	0%	-7%	-69%	80%	39%
<b>Hop Inn budget hotels (Thailand)</b>	<b>2018</b>	<b>2019</b>	<b>2020F</b>	<b>2021F</b>	<b>2022F</b>
Number of rooms	2,810	3,383	3,861	4,325	4,325
Occupancy rate	75%	73%	55%	67%	73%
ARR (THB)	580	609	548	548	576
% growth	7%	5%	-10%	0%	5%
RevPar (THB)	438	444	301	366	422
% growth	8%	1%	-32%	21%	15%

Source: Company data, RHB

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Figure 3: Erawan's 3Q20 and 9M20 performance preview

FYE Dec (THBm)	3Q19	2Q20	3Q20F	YoY % chg	QoQ % chg	9M19	9M20F	YoY % chg	Remarks
Revenue from hotel operations	1,441	56	396	-72.5	602.8	4,483	1,614	-64.0	All 22 properties under the non-Hop Inn hotel segments resumed operations in August, vs six hotels in July. It earned c.TH60m from the Government's "Let's Travel Together" campaign in Q3.
Turnover	1,498	79	421	-71.9	429.5	4,652	1,711	-63.2	
Gross profit	567	(327)	(133)	n.m.	n.m.	1,859	(102)	n.m.	Despite cost-savings programmes, fixed expenses remained and turned its EBIT and EBITDA into the red.
EBIT	186	(523)	(327)	n.m.	n.m.	721	(819)	n.m.	
EBIT margin (%)	12.4	(658.5)	(77.7)			15.5	(47.9)		Accounting impact of the Thai Financial Reporting Standard 16.
EBITDA	391	(260)	(83)	n.m.	n.m.	1,339	(49)	n.m.	
EBITDA margin (%)	26.1	(327.7)	(19.7)			28.8	(2.9)		Adverse impact of the pandemic to hotel revenue, and increasing costs post-hotel resumption may be major contributors to the net loss.
Interest expense	(102)	(135)	(120)	17.9	-10.9	(297)	(394)	32.4	
Pretax profit	84	(658)	(447)	n.m.	n.m.	423	(1,213)	n.m.	
Tax	(28)	8	2	n.m.	n.m.	(100)	11	n.m.	
Core profit	43	(625)	(426)	n.m.	n.m.	288	(1,154)	n.m.	
Net profit	43	(625)	(426)	n.m.	n.m.	270	(1,154)	n.m.	
Gross margin (%)	37.9	(411.4)	(31.7)			40.0	(6.3)		
SG&A/sales (%)	26.5	239.0	48.0			25.7	(42.9)		
Net margin (%)	2.8	(787.2)	(101.3)			5.8	(67.4)		
<b>Key indicators</b>									
<b>Total group excluding Hop Inn</b>									
Total hotel rooms	4,832	5,343	5,343	10.6	0.0	4,832	5,343	10.6	No openings of new hotels in 3Q20.
Occupancy rate (%)	74	1	13	-61.0	12.0	78	24	-54.0	Average occupancy rates ramped up from 9% in July, to 13% in August and c.18% in September. There may be high demand during the weekends and public holidays at its properties in Pattaya and Hua Hin.
ARR (THB/day)	2,470	1,216	1,359	-45.0	11.7	2,540	1,778	-30.0	Attractive promotional campaigns to draw guests.
RevPar (THB/day)	1,824	13	177	-90.3	1,258.5	1,990	249	-87.5	
<b>Hop Inn (excluding Hop Inn Philippines)</b>									
Total hotel rooms	3,146	3,462	3,462	10.0	0.0	3,146	3,462	10.0	With the main guests being domestic travelers, Hop Inns have proven to be the most resilient segment during the crisis, with the average occupancy rate almost back to normal.
Occupancy rate (%)	71	23	67	-4.0	44.0	72	52	-20.0	
ARR (THB/day)	604	581	613	1.5	5.5	602	600	-0.3	Still be able to command higher room rates; ie Hop Inn Hua Hin.
RevPar (THB/day)	428	136	411	-4.0	202.0	436	312	-28.4	

Source: Company data, RHB

## Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2020-08-20	Sell	2.5	3.2
2020-04-08	Sell	2.1	3.1
2020-01-14	Buy	7.3	5.4
2019-09-20	Buy	8.0	5.6
2019-03-06	Buy	9.2	7.3
2018-04-12	Buy	10.0	8.3

Source: RHB, Bloomberg

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