

Research Update

Cathay Number One Real Estate Investment Trust Ratings Affirmed At 'twA-/twA-2'; Outlook Stable

November 26, 2021

Rating Action Rationale

Taiwan Ratings Corp. today affirmed its 'twA-' long-term and 'twA-2' short-term issuer credit ratings on **Cathay Number One Real Estate Investment Trust** (Cathay No.1 REIT). The outlook on the long-term rating is stable. The ratings on Cathay No.1 REIT continue to reflect the trust's satisfactory asset quality and conservative financial policy relative to those of other Taiwan-based REITs. Cathay No.1 REIT's high asset and tenant concentration as well as its focus on the hotel industry temper these strengths. We believe the operating risks associated with hotels are higher than those for office buildings due to greater performance volatility driven by tourism activity. This is indicated by the adverse impact of the lockdown and international tourist restrictions on hotel operations in Taipei in response to the COVID-19 pandemic.

Outlook

The stable rating outlook on Cathay No.1 REIT reflects our expectation that the trust can maintain a ratio of debt to EBITDA below 9.5x over the next two years. This is despite our view that the trust's EBITDA will decline by 5%-10% in 2021, due to stalled international tourism and the lockdown in Taiwan in mid-2021. We view the cash flow dent to be a one-off event, and we believe the trust's rental income will rebound substantially in 2022 amid a recovery in domestic economic activity in the post-pandemic era, underpinned by the trust's stable base rent from Sheraton Hotel. The outlook also reflects the trust's conservative financial policy, aimed at maintaining the ratio of debt to assets below 25%, which should constrain its debt level and help to keep the ratio of debt-to-EBITDA commensurate with the rating on the REIT.

Downward scenario

We could lower the rating on the trust over the next one to two years if:

- the ratio of debt-to-EBITDA increases to more than 9.5x, possibly due to an aggressive debt-financed asset acquisition with a lower-than-expected return; or
- the trust's cash flow volatility exacerbates, possibly due to tenant turnover at its key asset or a material and persistent decrease in rental income, which could result from a sharp and prolonged downturn in Taipei's tourism market.

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Upward scenario

We could raise the rating on the trust if:

- the trust could reduce the volatility of its revenue, possibly brought by a more diversified asset portfolio after the completion of urban renewal of Taipei Chunghwa Building, which could provide a stable rental stream to mitigate the trust's currently higher rental volatility. Stable EBITDA and return on capital through economic downturns by managing the risk associated with its single-asset concentration and hotel-dominant portfolio could indicate such improvement. At the same time, the trust would have to maintain a financial policy that keeps its debt-to-asset ratio no higher than 25%.

Related Criteria & Research

Related Criteria

- General Criteria: Methodology For National And Regional Scale Credit Ratings - June 25, 2018
- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings - October 10, 2021
- General Criteria: Group Rating Methodology - July 01, 2019
- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments - April 01, 2019
- Criteria | Corporates | General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers - December 16, 2014
- General Criteria: Country Risk Assessment Methodology And Assumptions - November 19, 2013
- General Criteria: Methodology: Industry Risk - November 19, 2013
- Criteria | Corporates | General: Corporate Methodology - November 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities - November 13, 2012
- General Criteria: Principles Of Credit Ratings - February 16, 2011

Related Research

- Taiwan Ratings' Ratings Definitions – August 10, 2020

(Unless otherwise stated, these articles are published on www.taiwanratings.com)

Ratings List

Ratings Affirmed

Cathay Number One Real Estate Investment Trust

Issuer Credit Rating	twA-/Stable/twA-2
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Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.taiwanratings.com for further information. Complete ratings information is available to subscribers of Rating Research Service at rrs.taiwanratings.com.tw. All ratings affected by this rating action can be found on Taiwan Ratings' public website at www.taiwanratings.com.

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