Media Release:

Fubon No.1 REIT Ratings Affirmed At 'twA+/twA-1' On Likely Asset Expansion; Outlook Stable

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Rating Action Overview

- We expect **Fubon Number One Real Estate Investment Trust** (Fubon No.1 REIT) to expand its asset portfolio over the next few months.
- We lowered our assessment of the trust's financial risk profile to significant from modest previously, due to a potential increase in the post-acquisition ratio of debt to EBITDA. We also raised our financial policy assessment to neutral from negative, given the trust's limited headroom to take on additional debt.
- At the same time, we lowered our liquidity assessment to adequate from exceptional to reflect the significant amount for new asset acquisitions to be fully funded by debt.
- We affirmed our 'twA+/twA-1' issuer credit ratings on Fubon No.1 REIT.
- The stable rating outlook reflects our view that the trust's satisfactory asset quality, stable cash flow generation, and disciplined financial policy should maintain the ratio of debt to EBITDA below 11x over the next one to two years.

Rating Action Rationale

Potential acquisitions could significantly raise debt leverage and nearly exhaust additional borrowing capacity. We anticipate the trust will spend new Taiwan dollar (NT$) 2.5 billion-NT$3.0 billion to acquire new assets over the next few months. The transactions will be fully debt-funded, which could raise the debt-to-EBITDA ratio to 9x to 10x post-acquisition, from 2x to 3x currently, after accounting for full-year rental income. However, the acquisitions will likely leave the trust with limited capacity to take on additional debt, given the trust's borrowing capacity is limited by local regulations at a ratio of total debt to total assets of below 35%).

The limited size of the new assets will only moderately improve the scale and diversification of the trust's asset pool. We continue to view Fubon No.1 REIT's asset portfolio quality as satisfactory. This reflects the good location and proper maintenance of its properties, which are in major business districts in Taipei City and benefit from relatively stable demand. Additionally, the strong creditworthiness of major tenants, particularly the Fubon Financial Holding Co., Ltd. (Fubon FHC) group, supports the REIT's stable rental income and sustainably high occupancy. However, the limited number of properties held by the trust, the high rental contribution from group companies, and the properties' concentrated geographic locations expose the REIT to concentration risk.

The acquisition of the new properties could moderately improve the REIT's asset profile by expanding its portfolio and enhancing diversification. This is despite our view that the potential acquisitions could slightly dilute the REIT's returns due to potentially lower gross yields under current market conditions and higher interest rates. Nonetheless, the relatively small size of the potential new assets is not enough to raise our assessment of the trust's business risk profile.

The revised liquidity score reflects the one-off impact of new acquisitions and zero rating impact. We revised our assessment on the trust's liquidity to adequate from exceptional based on our expectation that the liquidity sources over the next 12 months will include the additional debt required for the purchase of the new assets. However, the trust's liquidity uses will also include an equivalent amount for the value of the new assets. As a result, the ratio of liquidity sources to liquidity uses will decrease to 1.2x-1.5x, compared to our previous estimate of over 4x. The revision of the liquidity score is neutral to the ratings.

In addition, we revised our assessment of the trust's capital structure to negative from neutral to account for the trust's debt maturity profile, which fell to below three years because its existing debts will mature in 2026. Nevertheless, we view the trust's refinancing risks are limited, given its satisfactory credit standing and high-value assets available for collateral. Accordingly, we believe Fubon No.1 REIT's shorter debt maturity does not affect the ratings.

Outlook

The stable rating outlook reflects our view that Fubon No.1 REIT's satisfactory asset quality, low financial leverage, and association with the Fubon FHC group will support its credit quality over the next one to two years. The outlook also reflects our view that the trust's ratio of debt to EBITDA will remain below 11x over the same period.

Downward scenario

We could lower the long-term rating on Fubon No.1 REIT if:

- The REIT's debt-to-EBITDA ratio increases to more than 11x for an extended period. Such an increase could result from aggressive debt-financed asset acquisitions, high tenant turnover, or a sharp reduction in rental rates; or
- The trust's asset quality or profitability deteriorates materially, possibly due to much weaker performance by key tenant RT-Mart than under our current base case suggests, which leads to lower rental collection or even early termination.

Upward scenario

We could raise the rating if:

- The trust expands its asset base significantly and enhances diversification while maintaining its good asset quality, stable profitability, and debt-to-EBITDA ratio below 9.5x.

Our Base-Case Scenario

- Taiwan's real GDP to expand 3.0% in 2024 and 2.6% in 2025.
- Numerous new office spaces will enter the market in 2025-2026. However, robust demand for office space and the trust's solid asset quality should help sustain a moderate increase in rental rates.
- Cash outflow of NT$2.5 billion-NT$3.0 billion for new asset acquisitions in 2025, fully-funded by debt.
- Acquisition of new buildings will begin contributing rental income in the second quarter of 2025, contribute to 17%-20% rental income growth in 2025 and 4%-6% growth in 2026.
- Rental income from Fubon Dunbei building will remain largely flat over the next two years, underpinned by the building's stable and full occupancy. Revenue from the building's conference center to remain relatively stable after recovery of approximately 11% in 2023.
- Rental income from Fubon Chungshan building to increase 2%-4% in 2024 but remain largely flat in 2025, primarily driven by improved occupancy and mild upward revision in lease contract renewals.
- Rental income from Ruentex City Link Building to remain flat over the next two years, mainly due to long-term fixed base rent and stable tenant structure.
- Operating expenses will increase by about 15% in 2025 and another 3%-5% in 2026 for the expanded asset portfolio.

Fubon Number One Real Estate Investment Trust. – Taiwan Ratings Corp. Forecast Summary

Industry sector: Real estate investment trust and company

(Mil. NT$)	2022a	2023a	2024e	2025f	2026f
Revenue	401.9	411.5	413.9	489.7	515.3
EBITDA (reported)	271.6	280.2	280.6	340.4	360.7
EBITDA	271.6	280.2	280.6	340.4	360.7
Less: Cash interest paid	(20.8)	(22.1)	(19.9)	(50.5)	(84.1)
Funds from operations (FFO)	250.9	259.8	260.7	289.8	276.6
Cash flow from operations (CFO)	268.8	275.5	278.3	292.5	294.7
Capex	--	0.0	0.0	(2,700.0)	0.0
Free operating cash flow (FOCF)	268.8	275.5	278.3	(2,407.5)	294.7
Debt (reported)	1,807.7	1,770.3	1,731.8	4,392.4	4,392.4
Less: Accessible cash and liquid Investments	(1,023.5)	(995.4)	(996.7)	(1,006.7)	(1,041.5)
Debt	784.2	774.9	735.1	3,385.7	3,350.9
Cash and short-term investments (reported)	1,204.1	1,171.1	1,172.6	1,184.3	1,225.3
Adjusted ratios					
Debt/EBITDA (x)	2.9	2.8	2.6	9.9	9.3
Debt/debt and equity (%)	6.6	6.5	6.2	23.3	23.0
Annual revenue growth (%)	1.4	2.4	0.6	18.3	5.2
EBITDA margin (%)	67.6	68.1	67.8	69.5	70.0

All figures are adjusted by Taiwan Ratings Corp., unless stated as reported. Figures of forecast period are based on Taiwan Ratings Corp.'s base case scenario. a--Actual. e--Estimate. f--Forecast. NT$--new Taiwan dollar. N.M.--Not meaningful. Capex--Capital expenditure.

Liquidity

The short-term rating on Fubon No.1 REIT is 'twA-1', which reflects the long-term issuer credit rating and our assessment of the trust's adequate liquidity. This in turn reflects our estimate that the REIT's ratio of liquidity sources to liquidity uses will be 1.2x-1.5x for the next 12 months ending June 30, 2025, given our view that Fubon No.1 REIT has sufficient cash on hand and cash flow from operations to distribute its scheduled dividend. The trust's liquidity sources could continue to exceed uses, even if its EBITDA declined by 10%, because the REIT has a very low debt repayment compared to its cash on hand. We believe the trust's unpledged properties are an extra liquidity source, if needed. There is no financial covenant on the trust's borrowing.

Principal liquidity sources

- Cash and short-term investments of NT$1 billion as of the end of June 2024.
- Funds from operations of NT$275 million-NT$285 million for the 12 months ending June 2025.
- Newly raised debt of NT$2.5 billion-NT$3.0 billion for asset acquisition.

Principal liquidity uses

- Debt maturities of NT$35 million-NT$40 million annually for the 12 months ending June 2025.
- Cash dividend of NT$ 235 million-NT$245 million up to June 30, 2025.
- Assets acquisition of NT$2.5 billion-NT$3.0 billion.

Ratings Score Snapshot

Fubon Number One Real Estate Investment Trust		
	To	**From**
Issuer Credit Rating	twA+/Stable/twA-1	twA+/Stable/twA-1
Business risk	Satisfactory	Satisfactory
Country risk	Intermediate	Intermediate
Industry risk	Low	Low
Competitive position	Satisfactory	Satisfactory
Financial risk	Significant	Modest
Cash flow/Leverage	Significant	Modest
Anchor	twa+	twaa
Modifiers		
Diversification/Portfolio effect	Neutral (no impact)	Neutral (no impact)
Capital structure	Negative (-1 notch)	Neutral (no impact)
Financial policy	Neutral (no impact)	Negative (-2 notches)
Liquidity	Adequate (no impact)	Exceptional (no impact)
Management and governance	Neutral (no impact)	Neutral (no impact)
Comparable ratings analysis	Positive (+1 notch)	Neutral (no impact)
Stand-alone credit profile (SACP)	twa+	twa+
Note: The descriptors are on a global scale.		

Related Criteria & Research

Related Criteria

- Criteria | Corporates | Industrials: Key Credit Factors For The Real Estate Industry - February 26, 2018
- General Criteria: National And Regional Scale Credit Ratings Methodology - June 08, 2023
- Criteria | Corporates | General: Corporate Methodology - January 07, 2024
- Criteria | Corporates | General: Methodology: Management And Governance Credit Factors For Corporate Entities - January 07, 2024
- 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
- General Criteria: Principles Of Credit Ratings - February 16, 2011

Related Research

- Taiwan Ratings' Ratings Definitions – November 11, 2021

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

Ratings List

Ratings Affirmed	
Fubon Number One Real Estate Investment Trust	
Issuer Credit Rating	twA+/Stable/twA-1