

ABS/Taiwan  
New Issue

## Hung Tai Century Tower REAT

### Ratings

Class	Amount (NTDm)	Final Maturity	Rating	Note Type
A	1,765	June 2012	AAA(twn)	Fixed
B	355	June 2012	A(twn)	Fixed
C	250	June 2012	NR	Fixed
D	2,070	June 2012	NR	Residual

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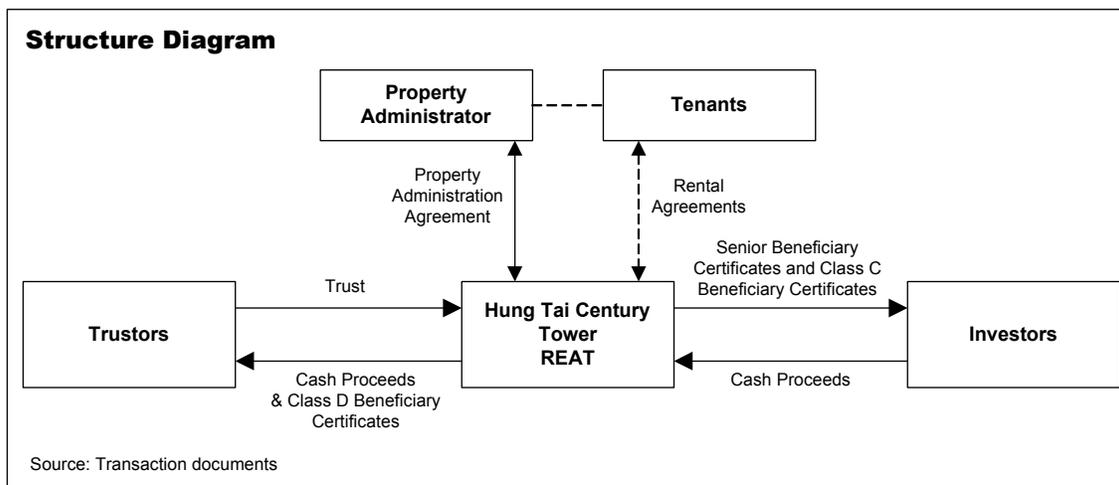
### Summary

Fitch Ratings has assigned ratings to the beneficiary certificates issued by a Real Estate Asset Trust (“REAT”) entrusted with part of the Hung Tai Century Tower (“HTCT”) as indicated at left. The ratings on the Class A and Class B beneficiary certificates (together, “the senior beneficiary certificates”) reflect the features of the underlying collateral and the integrity of the legal and financial structure of the senior beneficiary certificates. The ratings address the likelihood that investors will receive timely payment of interest and ultimate repayment of principal on the senior beneficiary certificates by legal final maturity in June 2012. The REAT also issued subordinated beneficiary certificates, Classes C and D, which are not rated.

The HTCT REAT was established under the Real Estate Securitisation Law enacted in July 2003 with the International Bank of Taipei as trustee. The property being transferred to the REAT includes 59 units (out of a total of 113) of the 19-storey office property known as the Hung Tai Century Tower, located in Dunhua North in central Taipei. The units are located on levels 10-19 and have a rentable area of 8,084.84 ping (approximately 26,720m<sup>2</sup>). It also includes 92 parking lots located on level B2, with a floor area of 1,751.41 ping (approximately 5,790 m<sup>2</sup>) and associated land area of 792.25 ping (approximately, 2,619m<sup>2</sup>). (together, “the entrusted property”). The entrusted property occupies approximately 40.6% of the entire HTCT. In exchange for the entrusted property, the owners, Chung Yi Construction Co., Ltd. (“Chung Yi”) and Fu Tai Construction Co., Ltd. (“Fu Tai”) (together, “the trustors”), will receive the cash proceeds from the issuance of the Class A, B, and C beneficiary certificates and ownership of the subordinated Class D beneficiary certificates.

### Strengths

- The entrusted property is located in the prime business district of Dunhua North and is easily accessible via various public transportation links, which are within walking distance. The property is also in close proximity to the domestic airport.
- The entrusted property has outperformed the market, distinguishing itself from the rest with occupancy rates averaging 97.6% over the past five years and currently standing at 100%; according to DTZ, the market average for the Grade A office property market in Taipei stood at 88% as of 1Q04.
- Notwithstanding the volatility of the rental market, where rental levels have fallen about 30% from their peak in 2000, the entrusted property has demonstrated relatively stable gross rental income over the past five years (gross office rental for the entrusted property dropped about 3% for 2003 compared to 2000).



- High lease renewal rates: more than 70% of existing tenants have been in the property for at least five years, thereby enhancing the stability of rental income.
- The availability of various reserves – the required liquidity reserve, the expense retention reserve and the low DSCR reserve – to provide liquidity and allow the transaction to trap excess cash if the performance of the cash flows is poorer than expected.
- The transaction structure incorporates an amortisation schedule that pays up to NTD60 million to the most senior beneficiary certificate then outstanding on each semi-annual payment date. This structure substantially mitigates the refinancing risk at expected maturity. Please note, however, that Fitch's rating does not address timely payment of the amortisation amount on each payment date.

### ■ Concerns

- Single-property concentration and a lack of geographical diversification.
- Tenant concentration: the top three tenants account for approximately 66% of gross rental income.
- The market vacancy rate is currently running at 12%, even prior to the imminent completion of Taipei 101 (at present the tallest building in the world). This building will add 58,000 ping of premium-grade office space to the Taipei market (or approximately 8% of total supply). The addition of so much space and the development of the Hsin Yi district as the new financial centre for Taipei will undoubtedly bring

downward pressure to bear on rents in Dunhua North.

- No earthquake insurance cover for the entrusted property.

### ■ Mitigants

- The entrusted property is in a prime location and is considered one of the best office properties in Taipei.
- The property has a base of high-quality tenants, the largest of which, Deloitte Touche Tohmatsu (including its affiliates and subsidiaries), currently contributes about 40% to gross rental income. Other major tenants include the Straits Exchange Foundation, NCR, GlaxoSmithKline and British American Tobacco. The trustors (one of which, Fu Tai, is retained as the property administrator) have enjoyed good and stable relationships with the tenants and have, in the past, received at least one year's advance notice of a tenant's decision to leave. An estimated period of three months is required to re-lease units.
- The property is located in a well-established sub-market with a mature transport infrastructure, as well as a network of shops, restaurants and other amenities. When calculating stabilised cash flows, Fitch has also taken into account potential downward pressure on rental income.
- Potential investors should consider the risk that an earthquake could affect the transaction. Fitch is informed that HTCT has been built in compliance with Taiwan's strict building code and is built to withstand an earthquake of up to

## Parties to the Transaction

**Issuer:** Hung Tai Century Tower REAT

**Trustors:** Chung Yi Construction Co. Ltd. and Fu Tai Construction Co. Ltd.

**Trustee/Account Bank:** International Bank of Taipei

**Property Administrator:** Fu Tai Construction Co. Ltd.

**Joint Arrangers:** Deutsche Bank AG, Taipei Branch and Capital Securities Corporation

**Lead Underwriter:** Deutsche Securities Asia Ltd., Taipei Branch

**Co-Lead Underwriter:** Capital Securities Corporation and Taiwan Cooperative Bank

## Transaction Highlights

**Entrusted Property:** the beneficiary certificates are ultimately backed by cash flows generated by the entrusted property as well as the land and property value.

### Minimum Fitch Stressed DSCR on Rated

**Debt:** 'AAA(twn)' (Class A) – 2.00x and 'A(twn)' (Class B) – 1.50x

### Debt Service Coverage on Rated Debt at

**Closing:** 'AAA(twn)' (Class A) – 4.6x and 'A(twn)' (Class B) – 3.8x

**Fitch Stressed Refinance Rate:** 8.25%

### Loan to Valuers' Value on Rated Debt:

'AAA(twn)' (Class A) – 39.8% and 'A(twn)' (Class B) – 47.8%

**Amortisation:** up to NTD60m on each payment date

**Expected Maturity Date:** December 2010

**Legal Final Maturity Date:** June 2012

7.0 on the Richter scale. During the "921" earthquake of 1999, the biggest in recent history, HTCT survived relatively unscathed, with only minor damage.

## Transaction Overview

The transaction relates to the entrustment of 59 of the 113 units of the HTCT, representing approximately 47.1% of the rentable office area, to the International Bank of Taipei ("IBT"). The trustors, Fu Tai and Chung Yi, are the owners of the entrusted property. IBT as trustee, will issue senior and subordinated beneficiary certificates backed by the entrusted property. The trustors will receive cash proceeds (net of transaction expenses and reserve amounts) from the issuance of the class A, B and C beneficiary certificates as well as ownership of the subordinated class D beneficiary certificate. The

beneficiary certificates have a seven-and-a-half-year legal final maturity and a six-year expected maturity.

Under the amortisation schedule for the beneficiary certificates, the most senior beneficiary certificates then outstanding will be repaid up to NTD60m on each payment date until its principal outstanding has been reduced to zero. However, Fitch's rating does not address the timeliness of this principal amortisation. Any amounts up to NTD60m that are not paid on a given payment date will be carried forward to the next.

At expected maturity, the trustors will redeem the entrusted property by redeeming the remaining outstanding principal of senior beneficiary certificates and the subordinated Class C beneficiary certificates plus accrued interest and expenses. At that time, the rights and benefits of the subordinated Class D beneficiary certificates, which are held by the trustors, will be extinguished. If the trustors do not redeem the certificates, the trustee will liquidate the entrusted property. The tail period of 18 months to legal final maturity will allow the trustee sufficient time to do so in an orderly manner.

## The Entrusted Property

The entrusted property and the cash flows it generates provide ultimate security for the rated beneficiary certificates. The HTCT is a Grade-A 19-storey office building located in the prime business district of Dunhua North. With a bus stop at its doorstep, a mass rapid transit station (Nanjing E. Road) within walking distance and the domestic airport in close proximity, the property gives tenants accessibility and convenience. Completed in 1991, the building has office units from levels 2-19 and accommodates a restaurant and a health club on B1. Parking facilities are located on levels B2 to B5.

The entrusted property comprises 8,084.84 ping of rentable office space located on levels 10-19 of the building and also includes 92 parking lots located on level B2. As of August 2004, the entrusted property was 100% occupied and average occupancy was 97.6% in the 1999-2003 period. The office units currently generate a gross monthly rental income of approximately NTD19m, while the parking lots generate approximately NTD828,000 per month.

The terms of the rental leases are standardised, generally involving three-year agreements and a security deposit of three months' rent. Tenants can terminate a lease early by giving three months' notice and forfeiting half of the security deposit. Lease ageing analysis indicates that leases on 41.2% of the office rentable area will expire in 2005, 7.1% in 2006 and 51.7% in 2007. These equate to 43.1%,

8.3% and 48.6% of gross monthly rental income, respectively.

The property has a base of high-quality tenants, the largest of which, Deloitte Touche Tohmatsu (including its affiliates and subsidiaries), currently occupies approximately 47.7% of the office rentable area. Other major tenants include the Straits Exchange Foundation, NCR, GlaxoSmithKline, British American Tobacco. The property's ability to retain tenants is evidenced by its high lease renewal rates: approximately 70% of existing tenants have been in the property for at least five years. These quality tenants enhance the stability of rents as they have substantial long-term office requirements.

Capital expenditure for the entire building is expected to amount to NTD53m for the 2005 to 2012 period. Capital expenditure requirements for the remainder of 2004 will be met prior to the closing of the transaction.

## ■ Property Administration

Fu Tai is one of owners of the entrusted property. IBT, as trustee, has contracted it to act as the property administrator pursuant to the property administration agreement.

Fu Tai is a subsidiary of the Hung Tai Group, which was established in 1975 and is one of Taiwan's largest private construction companies. Fu Tai, founded in June 1988, is involved in the lease and sale of commercial and residential properties in Taiwan.

As property administrator, Fu Tai will provide marketing and leasing, property management and maintenance services to the trust. Upon approval by the trustee and notice to Fitch, it may delegate part or all of its responsibilities to qualified third-party service providers. In the event of a breach of contract or obligation by the property administrator's delegates, Fu Tai will, along with its delegate, be liable to the trustee.

## ■ The Trust

A REAT was set up pursuant to the Real Estate Securitisation Law enacted in July 2003, a trust agreement and a real estate securitisation plan. The entrusted property is held on trust by IBT as trustee. The purpose of the REAT is to: (i) issue beneficiary certificates representing a beneficial interest in the entrusted property; and (ii) manage, dispose of, collect and distribute any interests in the entrusted property for the benefit of the certificate holders.

## ■ Fitch Cash Flow Analysis

Fitch visited the property, analysed its cash flow and held discussions with the management team. The agency also met the property valuers, Jones Lang LaSalle ("JLL") and DTZ Debenham Tie Leung ("DTZ"), as well as the tax advisor KPMG.

- The main focus of the analysis Fitch used to calculate its stabilised net cash flow was rental income/ping and occupancy rates. The current market average for Grade A office monthly rental in Taipei is approximately NTD2,000 per ping. Fitch believes excess supply in the market – especially with the introduction of Taipei 101 (due for completion in December 2004) – will bring downward pressure to bear on the HTCT's current in-place rent levels. However, when determining revenue cash flows for the term of the transaction, Fitch gave credit to HTCT's stabilised rent level by assigning a premium to the market average based on the property's position as one of the top-quality Grade A buildings in Taipei as well as the fact that it has historically tended to command rents above the market average. Furthermore, Fitch has given credit to current in-place rents to certain high-quality tenants for the duration of their lease agreements. The agency therefore applied an average overall haircut of approximately 12% to 2004 annualised gross rental income. When reviewing historical occupancy rates, Fitch assumed that the current 100% level was potentially unsustainable and therefore made an adjustment to reflect long-term stabilised levels, applying an average of approximately 19% haircut on 2004 annualised gross rental income for the purposes of its cash flow analysis.
- Car park income is currently generated by a single tenant, Da Yeh Enterprise Co., Ltd, which, in turn, manages and operates level B2 as a public hourly parking lot. Car park income was assumed at current levels, which marks a 40% reduction from its level in 2000.
- The tenants pay the property management fees and public utility expenses; where units are untenanted, the property administrator charges 50% of the property management fees and the trust is responsible for these fees.
- Property tax and land value tax expenses were assumed at the five-year historical high.
- Insurance premium expense reflects all risk insurance (excluding earthquake), rental loss coverage and third-party liability insurance.

- Capital expenditure assumptions are based on the recommendations of the independent engineer, CBRE.

## ■ Credit Issues

The ratings on the beneficiary certificates were influenced by the transaction's financial structure and collateral characteristics.

## Debt Service Coverage

Net operating income for the year ended December 2003 was approximately NTD223m, while Fitch's stabilised stressed net operating income was NTD181m – a haircut of 19%. Haircuts are less severe in earlier years of the transaction owing to the credit given to in-place rents, as described in the section *Fitch Cash Flow Analysis*. The agency's assumptions regarding the net cash flow available for debt service were calculated by deducting ongoing transaction expenses and forecast capital expenditures.

Fitch used a hypothetical mortgage refinance rate and debt service coverage ratios ("DSCRs") appropriate to each rating category to determine the maximum issue amount each class could support.

When analysing debt service coverage during the term of the transaction, Fitch applied indicative fixed rates of interest to the fixed-rate beneficiary certificates.

For refinancing, Fitch assumed that the total outstanding rated debt would be refinanced at a hypothetical rate of 8.25%. The refinance rate was calculated by reviewing 10 years of historical 90-day CP rates to determine a base rate, and adding an appropriate margin.

The refinance rate, together with the net cash flow available for debt servicing, determines whether cash flows would support the rated debt with the DSCRs deemed necessary for 'AAA(twn)' and 'A(twn)' ratings at the refinancing date.

The DSCRs deemed necessary for the rated beneficiary certificates are 2.0x and 1.5x, respectively, for 'AAA(twn)' and 'A(twn)' ratings.

## ■ Cash Management

Under the trust agreement, the trustee will set up a trust account to facilitate cash collections and distribution of the trust assets. The trust account will also be set up with the following sub-accounts.

- Collection account – this is used to collect rental payments, insurance proceeds and other income. Prior to closing, tenants will receive notice and

instructions to pay rent payments directly into the trust account, thereby mitigating any commingling risks.

- Security deposit account – this is set up to hold all security deposits paid by the tenants, which will be returned to them if they choose to terminate their leases upon expiration.
- Expense retention reserve account – this account will be funded at closing with an amount equivalent to 12 months of capital expenditure (the highest amount required within the term of the transaction) as recommended by CBRE, 12 months of land value tax, property tax and insurance premium.
- Reserve account – this account will be funded at closing with an amount equivalent to six months of interest for the Class A and B certificates and six months of ongoing fees for third-party service providers.
- Payment account – on each semi-annual payment date, payments due under the priority of payments will be made from this account.
- Low DSCR reserve account – if DSCR falls below 2.0x, the interest due to subordinated class D certificate holders will be trapped in this account and may be released only if the required DSCR level is restored.
- Tax reserve account – on any due date for various tax liabilities, amounts will be transferred from the collection account to the tax reserve account to pay withholding tax, business tax or other related taxes; amounts from the expense retention reserve account will also be transferred to the tax reserve account to pay land value tax and property tax.

Under the trust agreement, the trust account must be maintained with an institution rated at least 'F1(twn)' and 'A(twn)', or an institution otherwise acceptable to Fitch.

## ■ Insurance

The insurance providers will be Cathay Century Insurance Co., Ltd. and Fubon Insurance Co., Ltd. The trustee will be the named beneficiary for the benefit of the certificate holders. The insurance policies will include industrial all-risk insurance, rental loss insurance and third-party liability insurance. In addition to general exclusions such as war, terrorism, etc, the industrial all-risk insurance also excludes earthquake risk. Although Fitch understands that it is common practice not to take

out earthquake insurance in Taiwan owing to the costliness, potential investors should nonetheless be aware that earthquake risk has not been mitigated in this transaction. Rental loss insurance will cover up to 24 months of rental income loss caused by damages to the entrusted property.

The policy is renewed annually and must at all times be maintained with a provider rated at least 'A(twn)' or otherwise acceptable by Fitch.

The industrial all-risk insurance covers the replacement cost of the entrusted property, estimated by CBRE at NTD827.6m. The rental loss insurance covers a maximum rental of NTD485.5m. Insurance proceeds may, be used to pay interest and principal on the rated certificates if the restoration of the property cannot be completed six months prior to the expected maturity date.

## ■ Performance Analytics

Fitch will monitor the transaction on a regular basis and as warranted by events. Its structured finance surveillance team ensures that the assigned ratings remain, in the agency's view, an appropriate reflection of the issued notes' credit risk. Please call the Fitch analysts mentioned on the first page of this report for any queries regarding the initial analysis or the ongoing surveillance.

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