

Media Release:

Yulon Finance Corp. Upgraded To 'twA/twA-1' From 'twA-/twA-2' On Level Of Credit Insulation From Parent Group; Outlook Stable

February 10, 2020

Overview

- We assess that Yulon Finance has strengthened its governance structure, and we expect the company to achieve sufficient operational separation from the Yulon Motor group.
- Yulon Finance's stand-alone credit characteristics are superior to those of the parent group. We now view Yulon Finance as an insulated entity of the group, which allows for a one notch uplift to the issuer credit rating on Yulon Finance above the group credit profile.
- We are therefore raising our long- and short-term issuer credit ratings on Yulon Finance to 'twA/twA-1' from 'twA-/twA-2'.
- The outlook on the long-term rating is stable, reflecting the company's stable stand-alone credit profile, as well as the rating outlook on Yulon Motor.

Rating Action

Taiwan Ratings Corp. today raised its long- and short-term issuer credit ratings on **Yulon Finance Corp.** to 'twA/twA-1' from 'twA-/twA-2'. The outlook on the long-term rating is stable.

Rationale

The upgrade reflects our assessment that Yulon Finance has strengthened its governance structure by increasing the effective influence of its independent board members, and increasing the threshold of significant business /financial decision-making stated in its articles of incorporation. Under the new structure, we expect Yulon Finance to achieve sufficient operational separation from the parent Yulon Motor Co. Ltd. group. We now view Yulon Finance as an insulated entity of the parent group. Based on our assessment of the extent of the credit insulation, the issuer credit rating on Yulon Finance can be up to one-notch higher than the group credit profile.

Given that we assess Yulon Finance's stand-alone credit profile as superior to the group credit profile, the upgrade action more reflective of the financing company's stand-alone credit characteristics. We also believe the company's business and financial profiles offer a stable cushion against the potential impact of the current novel coronavirus outbreak.

PRIMARY CREDIT ANALYST

Eunice Fan
Taipei
+886-2-8722-5818
eunice.fan
@spglobal.com
eunice.fan
@taiwanratings.com.tw

SECONDARY CONTACT

Eva Chou
Taipei
+886-2-8722-5822
eva.chou
@spglobal.com
eva.chou
@taiwanratings.com.tw

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On Jan.20, 2020, Yulon Finance held an interim shareholders' meeting to add one more seat to the number of independent board members, which now exceeds one-third of the total seats on the board. At the same time, the company revised its articles of incorporation which requires that significant business or financial decisions need at least two-thirds of the directors present at the relevant board meeting, and at least two-thirds of the attendees concur with the proposal.

Under our previous rating assessment, the issuer credit rating on Yulon Finance was capped by the group credit profile, given the company's core group status through which we assessed its credit profile to be the same as that of the group. This is despite Yulon Finance's stand-alone credit profile is superior to the group credit profile. Under the new governance structure, we expect Yulon Finance to achieve sufficient operational separation from the parent group under which the independent directors have effective influence on major business and financial decision making. This could somewhat restrain the flow of Yulon Finance's resources to support other group members during periods of potential financial stress for the group.

We also believe that as a listed company, Yulon Finance holds itself as a separate entity with independent funding arrangements and has a good track record of fund raising. In addition, there is no material linkage between Yulon Finance's financial performance and that of the group, and we expect Yulon Finance to maintain good growth on its non-group related business over the coming one to two years. On consolidated basis, non-group business accounted for more than 90% of revenues and profits in 2018-2019, and the trend continues on an upward course as the company expands its used-car and corporate finance business. We therefore assess Yulon Finance has no significant business or operational dependence on the group.

We believe the Yulon Motor group has a strong economic incentive to preserve Yulon Finance's credit strength considering the finance and leasing company's high profit contribution and significant asset base under the group structure. Moreover, Yulon Finance is the group's sole auto finance provider, satisfying 80%-90% of Yulon Motor's new car installment needs. The company also provides auto-related, value-added services to Yulon Motor customers.

The ratings on Yulon Finance continue to reflect the company's strong business position in the domestic car financing and leasing sectors, strong capitalization relative to its risk profile, and adequate funding and liquidity profile. The company's moderate risk control framework compared to that of local banks somewhat tempers these strengths.

Outlook

The stable outlook reflects our expectation that Yulon Finance will maintain its strong market position in the domestic car financing and leasing sectors and strong capitalization over the next one to two years. We also expect its parent, Yulon Motor, to maintain a stable credit profile over the same period.

Downward scenario

We may lower the long-term rating on Yulon Finance if Yulon Motor's credit profile materially deteriorates, leading us to lower our assessment of the parent group credit profile. We could also lower the rating if Yulon Finance's stand-alone credit profile weakens, as indicated by

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consolidated risk-adjusted capital ratio below 10%, or if its asset quality substantially deteriorated.

Upward scenario

We may upgrade Yulon Finance if its stand-alone credit profile improves, particularly if it can sustain its capitalization at a very strong level as shown by a consolidated risk-adjusted capital ratio above 15% on a sustainable basis, while at the same time Yulon Motor improves its credit profile significantly. However, we view this to be remote over the next two years.

Related Criteria & Research

Related Criteria

- General Criteria: Hybrid Capital: Methodology And Assumptions - July 01, 2019
- General Criteria: Group Rating Methodology - July 01, 2019
- Understanding Taiwan Ratings' Rating Definitions - June 26, 2018
- Criteria | Financial Institutions | General: Risk-Adjusted Capital Framework Methodology - July 20, 2017
- Criteria | Financial Institutions | General: Nonbank Financial Institutions Rating Methodology - December 09, 2014
- Criteria | Financial Institutions | Banks: Quantitative Metrics For Rating Banks Globally: Methodology And Assumptions - July 17, 2013
- Criteria | Financial Institutions | Banks: Banking Industry Country Risk Assessment Methodology And Assumptions - November 09, 2011
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings - April 07, 2017
- General Criteria: Use Of CreditWatch And Outlooks - September 14, 2009

Related Research

- Full Analysis: Yulon Motor Co. Ltd. www.taiwanratings.com, November 13, 2019

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Ratings List

Upgraded

	To	From
Yulon Finance Corp.		
Issuer Credit Rating	twA/Stable/twA-1	twA-/Stable/twA-2

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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