Bulletin:

USI Corp.'s Improved Debt Leverage Is Barely Enough To Absorb COVID-19 Headwinds

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Taiwan Ratings Corp. said today that **USI Corp.'s** (twA-/Stable/twA-2) improved debt leverage provides only just enough buffer against likely weakening demand over the coming few quarters amid COVID-19.

Our current forecast indicates that USI's ratio of debt to EBITDA could rise to just over 3x in 2020, up from 1.9x in 2019. This takes into account a likely 15%-20% revenue decline and 20%-30% EBITDA decline in 2020 from the base in 2019. However, we expect the ratio to improve to 2.5x-3.0x in 2021 and later amid recovering operating cash flow and lower cash outflow for capital expenditure (capex) and investments. The ratio will remain narrowly stronger than 3x, a level that we believe to be adequate for our current rating on the company. We expect COIVD-19 to result in weakening market sentiment and business interruption, leading to weaker sales volume, lower product prices, and shrinking product spreads. However, under our baseline assumptions, solar power investments will likely accelerate after the pandemic subsides as governments try to stimulate their economies.

USI's operating performance in 2019 exceeded our previous expectation, mainly because of significant spread expansion on Ethylene-vinyl acetate (EVA) driven by robust demand in the second half of 2019. The company's cash flow strengthened further in the first quarter of 2020 benefitting from downward-trending feedstock costs as COVID-19 crushed demand for crude oil and many base chemicals. As of March 31, 2020, USI has lowered its ratio of debt to EBITDA (on a rolling twelve month basis) to 1.9x from 3.4x at the same time a year earlier. Nonetheless, a prolonged virus outbreak could cause a greater negative impact on the global market resulting in high downside risk for product margins and downstream demand throughout 2020, especially for commodity chemicals.

USI's continued capital injection in to its joint venture in the Chinese port of Gulei and high capex in Taiwan could further pressure USI's debt leverage and cash flow over the coming few quarters. That's if USI's profitability falls materially below our expectation and the company does not adjust its capex schedule. We expect USI to inject New Taiwan dollar (NT$) 1.5 billion in to the joint venture in 2020, which together with planned capex of about NT$2.5 billion in 2020 for the construction of new ethylene storage tanks will keep USI's capital spending elevated throughout the year.

This report does not constitute a rating action.