Media Release:

# Cheng Shin Rubber Ind. Co. Ltd. Ratings Affirmed At 'twA/twA-1'; Outlook Stable

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## Rating Action Overview

- Taiwan based **Cheng Shin Rubber Ind. Co. Ltd.** is the world's 10th largest tire manufacturer with about NT$14.8 billion EBITDA for the first three quarters of 2021.
- As Cheng Shin's capital expenditure could remain low over 2022-2023, the company is likely to improve its debt-to-EBITDA ratio to close to 1x over the period. Accordingly, we revised our financial risk profile assessment to modest from intermediate. However, given Cheng Shin's relatively volatile operating performance mostly resulting from business concentration in China, we revised the comparable rating analysis to negative from neutral. But the stand-alone credit profile remains unchanged at 'twa'.
- Taiwan Ratings Corp. today affirmed its 'twA' long-term and 'twA-1' short-term issuer credit ratings on Cheng Shin.
- The outlook on the long-term rating is stable.

## Rationale Action Rationale

*Cheng Shin's lowering debt level supports our assessment of stronger financial risk profile.* Cheng Shin should be able to keep its capital expenditure at very low level and make prudent cash dividend payments over 2022 to 2023. This will support the company to generate positive free cash flow of New Taiwan dollar (NT$) 5 billion-NT$10 billion per year and improve its ratio of debt to EBITDA to close to 1x over the period. Cheng Shin could lower its annual capital expenditure (capex) to NT$4 billion-NT$6 billion, from NT$8 billion-NT$12 billion per year over past few years, given its current still low utilization amid weakened demand. The capex will be mostly for equipment updates, with small amounts allocated for capacity additions for bicycle tires in Taiwan and motorcycle tires in Indonesia.

*Business concentration in China continues to weigh on Cheng Shin's overall performance*. The company will continue to face stiff competition in China, particularly in its passenger car and truck and bus businesses. This will keep the pressure on the company's utilization and profitability over the next two years. Cheng Shin's overall operating performance could also see some challenges from several uncertainties throughout 2022 including COVID constraints, supply chain disruptions, and chip component shortages. As a result, the supply-demand condition could deteriorate with intensifying market competition and depress Cheng Shin's overall performance, given China will still account for 50%-60% of Cheng Shin's sales over the next two to three years.

## Outlook

The stable rating outlook reflects our expectation that Cheng Shin will maintain its EBITDA margin at moderately above 20% and debt-to-EBITDA ratio closed to 1x over the next 12-24 months. This is despite the company's weakened business risk profile dragged by lower revenue, which we attribute to the pandemic impact over the past few years. We expect the company to benefit from the relatively sustainable auto market demand in China. However, high market uncertainties because of supply chain disruptions, as well as potential downside risk of a chip shortage could limit Cheng Shin's ability to meaningfully recover its business scale.

### Upward scenario

We may raise the rating if:

- Cheng Shin meaningfully restores its sales growth and strengthens its profitability over the next two years, as reflected in a recovery in sales of passenger car tires in China as well as by higher utilization in other product lines; and
- Simultaneous improvement in Cheng Shin's free cash flow generation and a reduction in debt to sustain the debt-to-EBITDA ratio materially below 2x. This could be achieved if the company lowered its working capital needs or cash dividends without making further aggressive capacity expansion.

### Downward scenario

Conversely, we may lower the rating if:

- Cheng Shin's profitability and cash flow weaken materially, or if the company takes on more aggressive capex than we previously expected. A ratio of debt to EBITDA above 2.5x on a sustainable basis would indicate such deterioration. The possible scenarios include rising competition on Cheng Shin's key market in China or failure to penetrate the new tire market for electric vehicles; or
- The company fails to maintain its cost competitiveness or brand strength. A substantial decline in Cheng Shin's EBITDA margin driven by the weakening average selling price of passenger car tire and truck and bus tire compared to its peers. An EBITDA margin below 15% for an extended period would indicate such deterioration.

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## Ratings Score Snapshot

Issuer Credit Rating: twA/Stable/twA-1

Note: The descriptors below are on a global scale.

Business risk: Fair

- Country risk: Moderately high
- Industry risk: Moderately high
- Competitive position: Fair

Financial risk: Modest

- Cash flow/Leverage: Modest

Anchor: twa

Modifiers

- Diversification/portfolio effect: Neutral (no impact)
- Capital structure: Neutral (no impact)
- Financial policy: Neutral (no impact)
- Liquidity: Adequate (no impact)
- Management and governance: Fair (no impact)
- Comparable rating analysis: negative (-1 notch)

Stand-alone credit profile: twa

# 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** | |
|---|---|
| **Cheng Shin Rubber Ind. Co. Ltd** | |
| Issuer Credit Rating | twA/Stable/twA-1 |