Media Release:

Yang Ming Marine Transport Corp. Upgraded To 'twA-/twA-2' On Robust Cash Flow; Outlook Stable

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Rating Action Overview

- **Yang Ming Marine Transport Corp.** generates the bulk of its revenue from long-haul routes. The company generated funds from operations of new Taiwan dollar (NT$) 216.7 billion in 2021.
- Continued congestion at key ports and disruptions in worldwide logistics caused by the COVID-19 pandemic have kept freight rates elevated and strengthened Yang Ming's profitability beyond our previous projection for 2022 and 2023. Meanwhile, Yang Ming's debt could decline further supported by continued strong operating performance and moderate capital expenditure (capex) in 2022-2023.
- We have raised our issuer credit ratings on Yang Ming to 'twA-/twA-2' from 'twBBB+/twA-2'.
- The rating outlook is stable to reflect our view that Yang Ming's strong operating cash flow could help to reduce its debt and strengthen its overall credit metrics over the next 12 months.

Rating Action Rationale

Elevated freight rates could sustain Yang Ming's revenue in 2022. Port congestion and disruptions to logistics globally continue to constrain global container shipping capacity. We believe that these issues along with the conflict between Russia and Ukraine could continue to support full-year average freight rates without quick corrections, despite economic headwinds from high inflation and rising interest rates. We project the company's weighted average freight rates from its main service routes will remain at the level capable of generating an even higher profit margin in 2022 compared to 2021.

Yang Ming's current financial strength can sustain its aggressive capex needs and further reduce its debt over the next one to two years. We anticipate the company's capex needs will soar over the next two years, reflecting the company's plans for newly built vessels mainly for long-haul service lines. We believe that Yang Ming continue to reflect uncertainty over the negative impact of global environmental rules on shipping via the scheduling of its chartered-in and owned vessels over the next one to two years. We believe Yang Ming's operating cash flow can outweigh its capex needs over the next same period, given the company's current strengthened profitability. In our base case, we project Yang Ming will generate stronger funds from operations than we believe is sufficient to cover its debt maturing in 2022.

Uncertainty remains over the company's high margin performance once the current industry cycle peaks. We anticipate that Yang Ming can establish even stronger revenue and margins in 2022 compared to 2021; however, we project its weighted average freight rate will gradually revert to the historical average level after the current wave of strong demand from developed countries fades and global port and inland infrastructure operations recover. We forecast Yang Ming's margin performance will return to normal and remain so after the marine cargo industry retreats from the peak.

Outlook

The stable rating outlook reflects our view that Yang Ming can use its strong profitability and cash flow to lower the company's debt over the next 12 months. Strong freight rates will support this paydown. The outlook also reflects our view that Yang Ming's role and linkage to the Taiwan government will remain intact and that the company will continue to have good access to Taiwan's banking channels over the next two years.

Downward scenario

We could lower the long-term rating on Yang Ming if:

- The company's competitive position weakens substantially, which could result from (1) a significant decline in the company's market share; or (2) a major deterioration in the company's cost structure and service network relative to larger peers' due to its inadequate fleet;
- Yang Ming's ratio of funds from operations (FFO) to debt falls below 45% for an extended period. This could result from aggressive debt-funded capex or aggressive cash dividend payments with prolonged deterioration in industry conditions, or weakening cash flow generation as freight rates plunge; or
- We believe the company's role and link to the Taiwan government has weakened substantially, which includes a substantial reduction in government ownership or control of Yang Ming's board. Nevertheless, we view this scenario as remote over the next one to two years.

Upward scenario

The likelihood of an upgrade over the next 12 months is limited because of Yang Ming's limited market position and high industry risk, along with a likely industry normalization that could slow Yang Ming's cash flow generation significantly. Nevertheless, we may raise the rating if:

- Yang Ming can sustain its strong operating cash flow and profitability through strengthened cost competitiveness and scale economies, or if the company maintains a conservative financial policy on capex and cash dividends that keeps its debt from rising significantly through business cycles, such that the ratio of FFO to debt rises substantially above 60% through business cycles.

Our Base-Case Scenario

Yang Ming's revenue could grow steadily by more than 20% in 2022, reflecting high freight rates over the period. However, we forecast the carrier's revenue could decline by 40%-45% in 2023 reflecting a decline in freight rates amid normalizing market conditions. Our base-case assumptions for Yang Ming are:

- S&P Global forecasts Asia Pacific's real GDP will expand by 2.8% in 2022 and 2.6% in 2023 and for U.S. real GDP to grow by 3.2% in 2022 and 1.1% in 2023.

- Yang Ming's total capacity to remain stable with the negative effect of new environmental rules offsetting additional capacity from new and chartered in vessels offset over the next one to two years. The company could maintain its loading rates in 2022 to meet trade volumes for its four main service routes.
- The company's average freight rate to increase by 20%-40% year on year in 2022. Upward pressure on freight rates could abate over the next one or two years with Yang Ming's average freight rate declining 40%-50% in 2023.
- While Yang Ming's unit operating costs could go down in 2022 due to prudent cost efficiency management, the unit bunker fuel price could increase to US$620-US$680 per ton in 2022 due to rising oil prices.
- Yang Ming's operating leases to increase over the next one to two years, reflecting the company's ongoing vessel renewal and capacity addition plans, including five 11,000 twenty-foot equivalent unit vessels delivered in 2022 for its long-haul services.
- Yang Ming's capex could rise substantially in 2022, given the company's plans for new owned vessels and containers. We project capex for 2022 at more than NT$10 billion for new vessels and NT$5 billion–NT$8 billion on containers.
- Yang Ming to maintain its stable dividend payout policy over the next two years.

Based on these assumptions, we arrive at the following credit measures:

- EBITDA margin in 2022-2023 exceeding the actual level in 2021.
- Debt free on an adjusted basis in 2022-2023 due to the company’s surplus cash position.

Liquidity

The short-term rating on Yang Ming is 'twA-2'. We see Yang Ming has adequate liquidity sources to cover its needs in the next 12 months ending December 2022, based on our forecast that the company's liquidity sources will cover 3.5x-4.0x of its liquidity uses without refinancing. Yang Ming should be able to cope with high-impact low-probability events with limited refinancing, given the company's high cash balance on hand, as well as relatively strong operating cash flow in 2022. As of the end of December 2021, Yang Ming has about NT$193.5 billion in cash and short-term investments. We believe Yang Ming has good access to banks underpinned by its connection with the Taiwan government.

Principal liquidity sources

- Cash and short-term investments of NT$193.5 billion as of the end of December 2021.
- Cash flow from operations of NT$200 billion-NT$260 billion in 2022.
- Undrawn bank lines maturing beyond 12 months of about NT$8.8 billion in 2022.

Principal liquidity uses

- Debt maturity of NT$10 billion-NT$14 billion in 2022.
- Current operating lease of NT$10 billion-NT$13 billion in 2022.
- Capex of NT$21 billion-NT$27 billion in 2022.
- Cash dividends payment of NT$69.8 billion in 2022.

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
- General Criteria: Rating Government-Related Entities: Methodology And Assumptions - March 25, 2015
- 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

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Ratings List

Upgraded

	To	From
Yang Ming Marine Transport Corp.		
Issuer Credit Rating	twA-/Stable/twA-2	twBBB+/Positive/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.