中華信用評等
Taiwan Ratings
An S&P Global Company

Rating Research Service
信用評等資料庫

Bulletin:

Extended Downturn Erodes Formosa Plastics Group Companies' Rating Buffers

October 12, 2022

PRIMARY CREDIT ANALYST

Raymond Hsu, CFA
Taipei
+886-2-2175-6827
raymond.hsu
@spglobal.com
raymond.hsu
@taiwanratings.com.tw

SECONDARY CONTACT

Irene Lai
Taipei
+886-2-2175-6825
irene.lai
@spglobal.com
Irene.lai
@taiwanratings.com.tw

Four key Formosa Plastics group companies can absorb the financial impact of weak profitability and operating cash flow over the next two to three quarters because of the group's strong capital structure.

That's despite a narrowing rating buffer on each of the Taiwan-based chemical and oil refining companies. Formosa Plastics Corp. (twAA/Stable/twaA-1+), Nan Ya Plastics Corp. (twAA/Stable/twaA-1+), Formosa Chemicals & Fibre Corp. (twAA/Stable/twaA-1+), and Formosa Petrochemical Corp. (twAA/Stable/twaA-1+) reported operating losses of about new Taiwan dollar (NT$) 18.2 billion in the third quarter of 2022. This was the result of inventory losses and thin product spreads stemming from high and volatile oil prices and ongoing COVID-19 curbs in China.

We anticipate China's zero-COVID policy, and an extended slump in the country's property market, will slow recovery in China's domestic demand for the rest of 2022. In addition, high inflation and interest rates will hurt exports and further undermine chemical demand in Asia. This, together with still elevated crude oil prices, could hinder a significant recovery in the four companies' profitability for the rest of 2022.

We now expect the four companies' aggregate EBITDA to decline to NT$150 billion-NT$160 billion in 2022. This is sharply lower than our previous forecast of NT$210 billion-NT$220 billion. The four companies' operating performance is likely to improve gradually in 2023. But weak demand and high oil prices will constrain the improvement.

The four companies' debt could rise faster in 2022 than our previous forecast, due to significant working capital outflow, higher dividend payments and capex, and weaker profitability.

The companies together reported working capital outflow of about NT$76 billion in the first half of 2022 because of rising oil prices and shipping bottlenecks. We also estimate that the four companies will pay cash dividends of about NT$150 billion in the third quarter of 2022.

Their ratio of debt to EBITDA will increase to about 2x in 2022-2023, from 0.6x in 2021. This is materially higher than our previous forecast of around 1x.

Despite the downside risk from uncertainty in the global economy, we forecast that the extended suspension of the four companies' chemical project in the state of Louisiana in the U.S., lower cash dividends, together with stabilizing profitability and operating cash flows, could prevent the four companies' credit metrics from further deterioration.

Tightening environmental requirements and sharp cost inflation in the companies' key operating regions, particularly in the U.S., make it difficult to pursue large scale chemical projects. The companies have responded by extending their investment time frames.

We now believe that construction of Formosa Petrochemical's Louisiana chemical project is unlikely to start earlier than 2024, even if the company overcomes regulatory hurdles and decides to resume the project. A delay would lead to lower capex in 2023-2024 than our previous assumption. We expect cash dividends to decrease sharply, along with lower profitability, based on our view that the four companies will maintain a stable payout ratio.

This report does not constitute a rating action.

Copyright © by Taiwan Ratings Corp. All rights reserved.

Copyright © 2022 by Taiwan Ratings Corporation (TRC). All rights reserved.

No content (including ratings, credit-related analyses and data, valuations, model, software or other application or output therefrom) or any part thereof (Content) may be modified, reverse engineered, reproduced or distributed in any form by any means, or stored in a database or retrieval system, without the prior written permission of TRC. The Content shall not be used for any unlawful or unauthorized purposes. TRC and any third-party providers, as well as their directors, officers, shareholders, employees or agents (collectively TRC Parties) do not guarantee the accuracy, completeness, timeliness or availability of the Content. TRC Parties are not responsible for any errors or omissions (negligent or otherwise), regardless of the cause, for the results obtained from the use of the Content, or for the security or maintenance of any data input by the user. The Content is provided on an "as is" basis. TRC DISCLAIMS ANY AND ALL EXPRESS OR IMPLIED WARRANTIES, INCLUDING, BUT NOT LIMITED TO, ANY WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR USE, FREEDOM FROM BUGS, SOFTWARE ERRORS OR DEFECTS, THAT THE CONTENT'S FUNCTIONING WILL BE UNINTERRUPTED OR THAT THE CONTENT WILL OPERATE WITH ANY SOFTWARE OR HARDWARE CONFIGURATION. In no event shall TRC be liable to any party for any direct, indirect, incidental, exemplary, compensatory, punitive, special or consequential damages, costs, expenses, legal fees, or losses (including, without limitation, lost income or lost profits and opportunity costs or losses caused by negligence) in connection with any use of the Content even if advised of the possibility of such damages.

Credit-related and other analyses, including ratings, and statements in the Content are statements of opinion as of the date they are expressed and not statements of fact. TRC's opinions, analyses and rating acknowledgment decisions (described below) are not recommendations to purchase, hold, or sell any securities or to make any investment decisions, and do not address the suitability of any security. TRC assumes no obligation to update the Content following publication in any form or format. The Content should not be relied on and is not a substitute for the skill, judgment and experience of the user, its management, employees, advisors and/or clients when making investment and other business decisions. TRC does not act as a fiduciary or an investment advisor except where registered as such. While TRC has obtained information from sources it believes to be reliable, TRC does not perform an audit and undertakes no duty of due diligence or independent verification of any information it receives. Rating-related publications may be published for a variety of reasons that are not necessarily dependent on action by rating committees, including, but not limited to, the publication of a periodic update on a credit rating and related analyses.

To the extent that regulatory authorities allow a rating agency to acknowledge in one jurisdiction a rating issued in another jurisdiction for certain regulatory purposes, TRC reserves the right to assign, withdraw or suspend such acknowledgement at any time and in its sole discretion. TRC disclaims any duty whatsoever arising out of the assignment, withdrawal or suspension of an acknowledgment as well as any liability for any damage alleged to have been suffered on account thereof.

TRC keeps certain activities of its business units separate from each other in order to preserve the independence and objectivity of their respective activities. As a result, certain business units of TRC may have information that is not available to other TRC business units. TRC has established policies and procedures to maintain the confidentiality of certain non-public information received in connection with each analytical process.

TRC receives compensation for its solicited ratings and certain analyses, normally from issuers, originators, arrangers, or underwriters of securities or from obligors. TRC reserves the right to disseminate its opinions and analyses. TRC's public ratings and analyses are made available on its Web sites, www.taiwanratings.com (free of charge), and rrs.taiwanratings.com.tw (subscription), and may be distributed through other means, including via TRC publications and third-party redistributors. Please click here for any other conflict of interests that may affect the credit rating as requested by the regulator.