Bulletin:

Wan Hai's Improved Capital Structure Can Absorb Falling Freight Rates

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This report does not constitute a rating action.

Taiwan Ratings Corp. today said that Wan Hai Lines Ltd. has built a net cash position to buffer against the plummet in seaborne freight rates since the second half of 2022.

Soaring demand for physical goods along with congested seaborne traffic during the pandemic had pushed up freight rates to record highs. This helped Taiwan-based operator Wan Hai (twA/Stable/twA-1) accumulate a high cash balance over the past two years. The enhanced cash position has provided material uplift to the operator's overall capital structure, enough to shield it from further weakening in freight rates over the coming few quarters, in our view.

Our base case for Wan Hai Lines supports our view of the operator's sustained net cash position over the next two years. This is despite a contraction in freight rates and increased capital expenditure for vessel replacement and capacity expansion. We forecast the company's blended freight rate will drop by about 50% in 2023 and further by 5%-10% in 2024, from a record peak at the beginning of 2022. The extent of decline in the freight rate on Wan Hai's all important intra-Asia route will be less, given more balanced supply and demand conditions in this region compared with long-haul routes. For more details, please see Related Research. At the same time, we assume bunker costs will decline to US$580-US$620 per ton in 2023, from US$680-US$720 per ton in 2022.

Under our stress scenario for Wan Hai, we assume a drop of about 80% in the company's blended rate from the peak in 2022. This would return the blended rate to about the pre-pandemic level in 2019. We forecast that if Wan Hai failed to pass through at least 60% of its incremental costs, its funds from operations would turn negative, but the company could still maintain a net cash position. A plunge of more than 90% in the blended rate would take the company into a net debt position.

However, we believe these stress scenarios are unlikely to occur, given Wan Hai's focus on profit and efficient capacity management. Moreover, the addition of newly built vessels could also help improve Wan Hai's operating efficiency and partly support the company's profitability over the next one to two years. Nonetheless, Wan Hai’s aggressive expansion in transpacific routes could bring volatility to profits, because competition is more intense on long-haul routes and Wan Hai is not part of a major container carrier alliance. Our ratings on Wan Hai could come under pressure if the company's long haul route expansion keeps its profitability persistently weak amid a lengthy market downturn or intense competition from larger peers.

Related Research

- Global Shipping 2023: Containerships And Tankers Part Ways, Feb. 7, 2023