

Media Release:

Ratings On Sercomm Corp. Affirmed At 'twA-/twA-2'; Liquidity Revised To Strong From Adequate; Outlook Stable

May 22, 2023

Rating Action Rationale

Taiwan Ratings Corp. today affirmed its 'twA-' long-term and 'twA-2' short-term issuer credit ratings on Taiwan-domiciled **Sercomm Corp.** The outlook on the long-term rating is stable.

The ratings on Sercomm reflect our view that the company's good software development capability coupled with hardware design and in-house manufacturing underpin its market position in the telecommunication equipment industry. In addition, the tech war between China and the U.S. as a result of the U.S. government's clean network program has significantly reduced competition for Sercomm from Chinese telecom equipment suppliers in the U.S. and Europe. However, Sercomm's limited pricing power against its powerful clients, relatively smaller operating scale, and less-favorable product mix with high contribution from low-margin businesses could continue to constrain the company's profitability and competitiveness.

The ratings also incorporate our view that Sercomm is underpinned by its stable operating cash flow generation and the company will continue to maintain its minimal debt leverage over the next two years.

We have revised our assessment of Sercomm's liquidity to strong from adequate, which has no impact on the ratings. The revision mainly reflects our view that the company's liquidity buffer has strengthened due to its increased cash balance, declining working capital needs and strengthened profitability, despite still-elevated capex and debt maturity.

Outlook

The stable outlook reflects our expectation that Sercomm could continue to expand its EBITDA and gradually lower its debt leverage over the next two years. The company's revenue growth is likely to slow down in 2023 amid economic deceleration, especially in the U.S. and Europe, but could pick up in the following years thanks to the ongoing broadband upgrade trend around the globe and the company's new product launches. However, Sercomm could maintain improved profitability due to better product mix. We also believe Sercomm will stay prudent in overseas investments for production base diversification without materially increasing its debt level.

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Downside scenario

We could lower the rating on Sercomm if:

- The company's ratio of debt to EBITDA ratio stays above 1.5x without any sign of improvement, possibly due to a lengthened cash conversion cycle that leads to significant debt-funded operating cash outflow to support revenue growth and high capex, including further production base diversification; or
- The company's ineffective R&D or product design, or intensified competition particularly from Chinese manufacturers, lead to a material loss of key customers, revenue, and margins.

Upside scenario

The rating upside is limited over the next two years, given Sercomm's still-high product concentration on lower-margin broadband customer premises equipment. However, we could raise the rating on Sercomm if:

- The company broadens the scope of its product offerings and diversifies its product mix such as a material increase in revenue from Internet of Things solutions to generate higher and more stable margins. Under this scenario, Sercomm could materially grow its revenue and EBITDA and, at the same time, sustain its above-industry-average return on capital.
- Meanwhile, Sercomm maintains its ratio of debt to EBITDA below 1.5x.

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 – Nov. 11, 2021

(Unless otherwise stated, these articles are published on www.taiwanratings.com)

Ratings List

Ratings Affirmed

Sercomm Corp.

Issuer Credit Rating	twA-/Stable/twA-2
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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.

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