

Media Release:

Far EasTone Telecommunications 'twA+/twA-1' Ratings Affirmed; SACP Revised Upwards On Improving Debt Leverage; Outlook Stable

January 18, 2024

Rating Action Overview

- **Far EasTone Telecommunication Co. Ltd.** is one of the three leading operators in Taiwan's oligopoly telecommunications market. Far EasTone formally merged with Asia Pacific Telecom Co., a small telecom operator, on Dec. 15, 2023.
- We have raised our assessment of Far EasTone's stand-alone credit profile (SACP) to 'twaa' from 'twaa-'. We base this on our view that the operator will continue to reduce its debt leverage to bring the ratio of debt to EBITDA down to 1.6x in 2024 and to 1.3x in 2025 from about 2.0x in 2022 and 2023.
- We have affirmed our 'twA+/ twA-1' issuer credit ratings on Far EasTone, given our view that the company will remain an insulated and strategically important subsidiary of **Far Eastern New Century Corp.** (FENC), one of the largest conglomerates in Taiwan.
- The stable rating outlook on Far EasTone reflects our outlook on FENC. This incorporates our view that Far EasTone's steady operating cash flow will help to contain the group's rising debt and cap the rise in the group's ratio of debt to EBITDA at 4.8x-5.2x over the next two years.

Rating Action Rationale

Strong positive discretionary cash flow should uplift Far EasTone's financial profile. We believe the additional debt that Far EasTone took on through the merger with Asia Pacific Telecom could elevate Far EasTone's post-merger debt to new Taiwan dollar (NT\$) 64 billion at the end of 2023. This compares with NT\$60 billion at the end of 2022. However, we forecast the company's debt will edge down to around NT\$55 billion in 2024 and decline further to NT\$46 billion in 2025, supported by Far EasTone's stable and sustainable cash flow from its core business. We have therefore revised upward our assessment of Far EasTone's financial risk profile to modest from satisfactory and raised the rating anchor to 'twaa' from 'twA+'. We revised our assessment of the company's comparable rating analysis to neutral from positive. That's because we believe that our assessment of the financial risk profile fully captures its strength thanks to the reduced leverage.

We anticipate Far EasTone will continue to see positive discretionary cash flow of NT\$10 billion-NT\$11 billion annually in 2024 and 2025. Satisfactory growth momentum in the average-revenue-per-user (ARPU) of its core mobile service business underpins our forecast. The increasing adoption of more expensive 5G data plans could support this growth.

PRIMARY CREDIT ANALYST

Beatrice Chen
Taipei
+886-2-2175-6829
beatrice.chen
@spglobal.com
beatrice.chen
@taiwanratings.com.tw

SECONDARY CONTACT

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

Far EasTone's positive discretionary cash flow should be sufficient to cover the company's capital expenditure (capex) needs resulting from the merger. It should also help maintain the debt-to-EBITDA ratio comfortably below 2.0x over the next two years. We believe Far EasTone will continue to deleverage in 2024 and 2025; however, potential large capex for the deployment of its 5G stand-alone network, 6G spectrum, or any additional investments could push its debt leverage higher.

We believe Far EasTone's competitive position will remain largely unchanged post-merger. Our assessment of the company's competitive position reflects the company's stable business profile, underpinned by its top three ranking in Taiwan's mobile sector. The merger with Asia Pacific Telecom could increase Far EasTone's market share to 30%-31%, up from 24% as of Nov. 30, 2023.

Improving pricing discipline as the industry consolidates should prevent further weakening in the operating performances of key players over next two to three years. That's despite our view that Asia Pacific Telecom's lower ARPU could dilute Far EasTone's post-merger EBITDA margin in the near term. Far EasTone has the highest 5G penetration rate among leading players, and we expect the company to maintain good growth momentum for its ARPU as more customers migrate to 5G services. Nonetheless, Far EasTone's higher business concentration in mobile services also results in a weaker market position than its integrated telecom peers.

Outlook

The stable rating outlook on Far EasTone reflects our assessment of the parent group credit profile, as well as Far EasTone's own financial profile. We expect the operator's relationship with the parent group to remain unchanged with no material decrease in the group's shareholdings over the next one to two years.

Downward scenario

We could lower the rating on Far EasTone if:

- We lower the parent group credit profile on a global rating scale. This may happen if the parent group's profitability deteriorates substantially or its capex exceeds our forecast significantly, such that the parent group's ratio of debt to EBITDA rises materially above 6x for an extended period. This could result from severe industry downturns or higher capex for major group businesses than we predicted. Higher capital spending could include greater cash outflows for mergers and a larger investment in green products, including recycled-PET, than we expected.

Upside scenario

We could raise the rating on Far EasTone if:

- We raise the group credit profile on the global rating scale. The most likely scenarios for this include improvement in the parent's ratio of debt to EBITDA to close to 4x on a sustainable basis. Sustainable and material improvement in the parent group's profitability and cash flow in its chemical business, prudent capex and dividend payouts, or a reduction in debt through asset disposals could result in such a scenario. The ratio of debt to EBITDA could also improve if the parent substantially enhances the competitive position of its purified terephthalic acid (PTA), polyester, and textile businesses by increasing product diversity and exposure to high-end products without impairing the group's debt leverage.

Our Base Case Scenario

- Taiwan's real GDP to grow 1.2% in 2023, 3.0% in 2024, and 2.6% in 2025.
- Far EasTone's revenue to increase by 5.1% in 2023 and 14.9% in 2024. This surpasses growth in Taiwan's GDP and is underpinned by rising ARPU, recovering tourist needs, and more rapid growth in the information communication technology (ICT) business. The higher growth in 2023 and 2024 also reflects the consolidation of Asia Pacific Telecom.
- Far EasTone's postpaid subscriber base (excluding the addition from Asia Pacific Telecom) to remain largely flat over the next two years, while the prepaid subscriber base will continue to benefit from the rise in international tourists in 2024-2025. Consolidation of Asia Pacific Telecom subscribers will increase Far EasTone's total subscriber base by 28%.
- We anticipate the blended ARPU of pre-merger Far EasTone to increase by another NT\$10-NT\$15 annually in 2024 and 2025 from NT\$596 at the end of November 2023, through an increase in 5G adoption and tourist demand recovery. However, the combined entity's ARPU is likely to decline in 2024, due to Asia Pacific Telecom's lower ARPU, which is nearly NT\$200 below Far EasTone's.
- Far EasTone's fixed-line revenue to grow by a low single digit in 2024 and 2025, underpinned by moderate growth in its ICT business.
- Far EasTone's EBITDA margin to remain nearly flat at 34.2% in 2023 compared with 34.5% in 2022. However, the margin could decline to 32.6%-32.8% in 2024 and 2025 due to Asia Pacific Telecom's lower EBITDA margin.
- Selling, general, and administrative expense to be 16%-18% of revenue in 2024-2025.
- Capex of NT\$9.5 billion annually for Far EasTone in 2024 and 2025.
- Cash dividend of NT\$10 billion-NT\$11 billion annually for 2024 and 2025.

Far EasTone Telecommunications Co. Ltd.--Forecast summary

Industry sector: Diversified telecom

(Mil. NT\$)	2021a	2022a	2023e	2024f	2025f	2026f
Revenue	85,320	89,151	93,690	107,608	109,655	111,626
EBITDA (reported)	28,170	30,792	32,587	33,524	33,976	34,708
Plus/(less): Other	--	0	(504)	1,812	1,812	1,812
EBITDA	28,170	30,792	32,082	35,336	35,788	36,520
Less: Cash interest paid	(678)	(665)	(870)	(797)	(650)	(519)
Less: Cash taxes paid	(2,024)	(1,945)	(2,504)	(2,525)	(2,447)	(2,413)
Funds from operations (FFO)	25,468	28,181	28,708	32,014	32,692	33,588
Cash flow from operations (CFO)	35,315	27,082	27,394	30,580	31,231	32,120
Capital expenditure (capex)	11,457	9,229	9,000	9,500	9,500	9,500
Free operating cash flow (FOCF)	23,859	17,853	18,394	21,080	21,731	22,620
Discretionary cash flow (DCF)	13,190	7,189	7,730	10,416	11,067	11,956
Adjusted debt	65,159	60,431	64,000	55,439	46,226	36,125
Cash and short-term investments (reported)	6,739	6,265	11,291	13,156	6,000	11,655
Adjusted ratios						
Debt/EBITDA (x)	2.3	2.0	2.0	1.6	1.3	1.0
FFO/debt (%)	39.1	46.6	44.9	57.7	70.7	93.0
DCF/debt (%)	20.2	11.9	12.1	18.8	23.9	33.1
Annual revenue growth (%)	7.3	4.5	5.1	14.9	1.9	1.8

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EBITDA margin (%) 33.0 34.5 34.2 32.8 32.6 32.7

All figures are adjusted by Taiwan Ratings Corp., unless stated as reported. a--Actual. e--Estimate. f--Forecast.

Liquidity: Adequate

The short-term rating on Far EasTone is 'twA-1', reflecting the long-term issuer credit rating and our assessment of the company's liquidity as adequate. We believe the company has sufficient liquidity to meet its needs up to September 2024, as indicated by a ratio of liquidity sources to liquidity uses of 1.85x over the same period. We also believe the operator can absorb high-impact, low-probability events, with limited need for refinancing, supported by the company's high cash balance.

In our view, Far EasTone has solid banking relationships and a very high standing in credit markets, as indicated by the low funding cost of its bank loans and bonds. The company issued 5-year bonds valued at NT\$2.3 billion in June 2023 and NT\$1.3 billion in July 2023, with coupon rates of 1.57% and 1.60%, respectively. Far EasTone has no financial covenants on its debts.

Principal liquidity sources

- Cash and short-term investments of about NT\$5.8 billion as of the end of September 2023.
- Funds from operations of NT\$30 billion for the 12 months ending September 2024.
- Undrawn mid-to-long term bank lines maturing beyond September 2024 of NT\$28.4 billion.

Principal liquidity uses

- Debt maturity of NT\$12.6 billion over the 12 months ending September 2024.
- Capex of NT\$9.4 billion for the period.
- Working capital outflow of NT\$2 billion over the period.
- Cash dividend of NT\$10.6 billion over the same period.

Ratings Score Snapshot

Far EasTone Telecommunications Co. Ltd.

Note: The descriptors below are on a global scale.

	To	From
Issuer credit rating	twA+/Stable/twA-1	twA+/Stable/twA-1
Business risk	Satisfactory	Satisfactory
Country risk	Intermediate	Intermediate
Industry risk	Intermediate	Intermediate
Competitive position	Satisfactory	Satisfactory
Financial risk	Modest	Intermediate
Cash flow/Leverage	Modest	Intermediate
Anchor	twaa	twA+
Diversification/portfolio effect	Neutral (no impact)	Neutral (no impact)
Capital structure	Neutral (no impact)	Neutral (no impact)
Financial policy	Neutral (no impact)	Neutral (no impact)
Liquidity	Adequate (no impact)	Adequate (no impact)
Management and governance	Neutral (no impact)	Neutral (no impact)

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Comparable rating analysis	Neutral (no impact)	Positive (+1 notch)
Stand-alone credit profile	twaa	twaa-
Group credit profile	twa	twa
Entity status within group	Strategically important	Strategically important

We assess Far EasTone as an insulated and strategically important subsidiary of the Far Eastern New Century group. The issuer credit rating on Far EasTone can be above the group credit profile but is subject to a cap of one notch above the group credit profile.

Related Criteria & Research

Related Criteria

- General Criteria: Group Rating Methodology - July 01, 2019
- Criteria | Corporates | General: Corporate Methodology - January 07, 2024
- Criteria | Corporates | General: Methodology: Management And Governance Credit Factors For Corporate Entities - January 07, 2024
- General Criteria: National And Regional Scale Credit Ratings Methodology - June 08, 2023
- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings - October 10, 2021
- 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
- Criteria | Corporates | Industrials: Key Credit Factors For The Telecommunications And Cable Industry - June 22, 2014
- General Criteria: Country Risk Assessment Methodology And Assumptions - November 19, 2013
- General Criteria: Methodology: Industry Risk - November 19, 2013
- 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

Far EasTone Telecommunications Co. Ltd.

Issuer Credit Rating	twA+/Stable/twA-1
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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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