Media Release:

Wiwynn Corp. 'twA/twA-1' Ratings Affirmed On Parent Group Deleveraging; Liquidity Revised To Exceptional; Outlook Stable

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Rating Action Overview

- **Wiwynn Corp.,** a subsidiary of Wistron Group, specializes in providing customized servers used in hyper-scale data centers. Wiwynn generated EBITDA of new Taiwan dollar (NT$) 16.9 billion in 2023.
- We have raised our assessment of the parent Wistron group credit profile supported by improving profitability and lower debt leverage. This also removes the cap on the long-term rating on Wiwynn at the current rating level.
- We have raised our liquidity assessment for Wiwynn to exceptional from adequate to reflect the company's reduced debt maturity over the next 24 months, along with strong profitability and abundant cash on hand following its global depository receipt and convertible bond issuance.
- We have affirmed our 'twA/twA-1' issuer credit ratings on Wiwynn.
- The stable outlook reflects our view that Wiwynn could resume revenue and EBITDA growth and maintain a net cash position over 2024-2025 amid booming demand for AI.

Rating Action Rationale

Our improved assessment of the parent group credit profile reflects our view that the group could deleverage significantly in 2024-2025. We forecast that Wistron's strengthening profitability and Wiwynn's recent global depository receipt issuance could help Wistron reduce its debt-to-EBITDA ratio to around 3x in 2024 and to 2.4x-2.7x in 2025, from 3.8x in 2023. This is because we believe that parent Wistron's strengthened cash flow generation could fund its capital expenditure (capex) needs and support the diversification of its production footprint while bringing down debt significantly in 2024-2025.

We forecast Wistron's capex will increase to NT$14 billion-NT$15 billion in 2024 from around NT$13 billion in 2023. It will use the capex to focus on capacity diversification away from China and into Taiwan, South-East Asia, and Mexico. This will help meet its clients' needs to mitigate geopolitical risk. In addition, we expect Wistron to continue invest in enhancing its technological capability but to keep this expenditure within the company's financial capability and without a material rise in debt.

We forecast Wistron's revenue could increase by 10%-15% in 2024-2025. This will mainly be driven by strong demand for AI-related products, including AI servers and GPU accelerator cards. Meanwhile, enterprise server shipments are also likely to recover in 2024 as companies accelerate their transition to the cloud. In addition, the introduction of AI-enabled models could facilitate a rebound in the shipment of notebook PCs in 2024-2025 following lukewarm demand in 2023. At the same time, Wistron's product transition to commercial applications (including Wiwynn) that could generate better and more stable profitability and the disposal of unprofitable business lines could better sustain the company's strengthened margins over the next two years.

The long-term rating on Wiwynn is no longer capped by the parent group credit profile. We continue to assess Wiwynn as an insulated and highly strategic subsidiary of Wistron Group. The issuer credit rating on Wiwynn can be one notch above the group credit profile on S&P Global Ratings' global rating scale, if Wiwynn's stand-alone credit profile is one or more notches above the group credit profile. This suggests that the rating on Wiwynn can reach 'twA+' before being capped by the group credit profile.

The insulated group status reflects our belief in Wistron's strategic need to maintain some separation from Wiwynn to avoid direct competition in the server market with its major generic server clients. In addition, Wiwynn is independent in its business operation and financial performance, and does not commingle its funds, other assets, or cash flow with Wistron's. However, we do not expect Wistron to fully divest Wiwynn, given the company's significant profit contribution and importance to the group's long-term strategy to develop its server business.

The ratings on Wiwynn continue to reflect the company's likely sustained market position and net cash position over the next two years. The rating affirmation reflects our view of Wiwynn's strong business position as one of the largest suppliers around the globe of tailor-made hyperscale data center servers by market share, and our expectation that Wiwynn will maintain a net cash position over the next two years. In addition, we see Wiwynn maintaining above-average profitability over the same period, given its efficient R&D and good operating efficiency boost demand for its tailor-made AI servers from key cloud service provider clients. We forecast that together with recovering demand for traditional servers from cloud service providers will help Wiwynn restore its revenue in 2024 to above the 2023 level.

In addition, we believe that Wiwynn's enhanced scale economy and rising sales of high-margin tailor-made AI servers will enable the company to improve its EBITDA margin to 8.0%-8.3% in 2024-2025 from 7.0% in 2023. Furthermore, we believe that Wiwynn's strengthening operating cash flow along with the NT$27.3 billion proceeds from the issuance of global depository receipts in July 2024 will enable it to maintain a net cash position in 2024-2025. That's despite our forecast of rapid growth in Wiwynn's working capital needs and heightened capex over the period.

Nonetheless, high customer and product concentration continues to constrain the ratings on Wiwynn. Under our estimate, the three biggest clients still accounted for more than 80% of Wiwynn's revenue in 2023. In addition, a lack of design and technology ownership leaves the company susceptible to rapid technology changes in the global server market and competition from players with a larger scale and more comprehensive product portfolios. This will in turn amplify Wiwynn's customer concentration risk in our view because the loss of any key client could result in significant business volatility. This is despite our forecast that Wiwynn's customer concentration will ease gradually, given its efforts to expand its client base.

Liquidity has grown stronger, supported by abundant cash on hand and reduced debt maturing over the next two years. We forecast Wiwynn's liquidity buffer will strengthen over the next two years. Several factors will support this, including the company's improving profitability, a decrease in debt maturing over the period, as well as proceeds from Wiwynn's global depositary share and NT$19.4 billion offshore convertible bond issuances in July 2024. This is despite the company's still-high capex needs and potential working capital outflow to support revenue growth in 2024-2025. Accordingly, we have revised our liquidity assessment for Wiwynn to exceptional from adequate.

Outlook

The stable rating outlook reflects our view that Wiwynn will continue to expand its EBITDA and maintain a net cash position in 2024-2025. Aggressive investments in AI infrastructure by its cloud service provider clients will drive Wiwynn's strong revenue growth over the next two years. Meanwhile, Wiwynn's capability in providing tailor-made products should enable it to slightly strengthen product margins over the same period.

Wiwynn's issuance of a global depository receipt in July 2024 will also enable it to maintain a net cash position in our view, despite heightened capex for overseas expansion and working capital needs. At the same time, we anticipate that Wistron will continue to lower its debt leverage over the next one to two years. The company's strengthened profitability underpinned by an improving product mix could help sustain the debt to EBITDA ratio below 3x in 2024-2025.

Downward scenario

We may lower the long-term rating on Wiwynn if:

- The debt to EBITDA ratio deteriorates to above 1.5x for an extended period. This could happen if Wiwynn becomes more aggressive on capex or investments than our base case suggests, or if the company's cash conversion cycle lengthens or profitability weakens materially, which leads to significant debt growth to fund working capital and capex needs; or
- Intense competition or deteriorating R&D strength relative to its peers induce severe margin pressure from its clients or the loss of key customers, which would indicate a material weakening in the company's competitive position. A weakening in Wiwynn's profitability, as measured by the return on capital falling to near 12%, would signal such a deterioration.

Upward scenario

We may raise the long-term rating if:

- Wiwynn expands its operating scale substantially by acquiring more market share in the hyper-scale data center server industry and by diversifying its customer base to lower the associated risk to cash flow volatility. At the same time, Wiwynn would need to sustain its enhanced profitability through the constant development of new products or technology faster than its peers.
- At the same time, Wiwynn would need to maintain the ratio of debt to EBITDA meaningfully below 1.5x; and
- Wistron maintains its credit quality without a material deterioration in its market position in the electronics manufacturing services and original design manufacturer industries as well as its profitability. At the same time, the company would need to maintain its ratio of debt to EBITDA below 3x.

Our Base-Case Scenario

- S&P Global's forecast for U.S. real GDP to grow by 2.5% in 2024 and 1.7% in 2025, Eurozone real GDP to grow by 0.7% in 2024 and 1.4% in 2025, and APAC real GDP to grow by 4.5% in 2024 and 2025.
- S&P Global's forecast for global IT spending to accelerate by 8.2% in 2024, following mild growth of 3.9% in 2023 under the global economic slowdown. This exceeds our expectation of global real GDP growth of 3.3% in 2024 and is mainly supported by cloud service providers' robust spending, particularly on AI infrastructure, as well as improving PC and smartphone shipments.
- We project Wiwynn's revenue to grow by 20%-25% in 2024 and 15%-20% in 2025 after a 17.4% decline in 2023, following aggressive procurement in hyper-scale data center server by major clients in preparation for generative AI-related development. Higher average selling price of AI servers than traditional ones also supports Wiwynn's revenue growth.
- We also anticipate gross margin to improve to 10.5%-10.8% in 2024-2025 from 9.8% in 2023, thanks to lower raw material prices, as well as Wiwynn's higher value added by providing design services for its clients' AI servers based on application-specific ICs.
- We project selling, general, and administrative expense to grow along with revenue in 2024-2025 with the R&D-to-revenue ratio at 1.3%-1.5% over the period.
- We expect capex to increase to NT$5.0 billion-NT$5.5 billion in 2024 from around NT$4.9 billion in 2023 but decline to NT$3.5 billion-NT$4.0 billion in 2025. The amount is mainly to support overseas capacity expansion in Malaysia, Mexico, and Taiwan, as well as for building Wiwynn's new headquarters in Taipei.
- Global depository share issuance of around NT$27.3 billion in July 2024.
- We project dividend payout ratio of 60%-65% of the previous year's net income in 2024-2025.

Wiwynn Corp.—Taiwan Ratings Corp. Forecast summary

Industry sector: Technology hardware

(Mil. NT$)	2021a	2022a	2023a	2024e	2025f	2026f
Revenue	192,625.9	292,876.0	241,901.0	296,085.3	340,498.1	391,572.8
EBITDA (reported)	11,934.9	18,595.9	16,872.7	24,068.1	28,018.8	31,438.5
EBITDA	11,934.9	18,595.9	16,872.7	24,068.1	28,018.8	31,438.5
Less: Cash interest paid	(334.2)	(886.3)	(926.5)	(846.4)	(543.0)	(188.4)
Less: Cash taxes paid	(2,708.9)	(2,344.9)	(5,165.8)	(4,862.0)	(5,755.3)	(6,519.6)
Funds from operations (FFO)	8,891.8	15,364.7	10,780.4	18,359.6	21,720.5	24,730.4
Cash flow from operations (CFO)	(27,270.9)	30,078.7	24,550.9	2,734.8	14,398.8	20,326.3
Capital expenditure (capex)	510.7	1,465.7	4,885.8	5,100.0	3,700.0	2,700.0
Free operating cash flow (FOCF)	(27,781.6)	28,613.1	19,665.1	(2,365.2)	10,698.8	17,626.3
Debt (reported)	30,716.0	9,448.1	11,333.3	8,833.3	4,108.3	390.4
Plus: Lease liabilities debt	671.0	1,013.2	1,521.0	2,283.2	2,511.5	2,511.5
Less: Accessible cash and liquid Investments	(22,219.4)	(25,812.2)	(33,895.3)	(47,496.1)	(43,295.0)	(44,502.5)
Plus/(less): Other	25,151.6	25,851.5	24,320.5	24,320.5	24,320.5	24,320.5
Debt	34,319.2	10,500.6	3,279.4	--	--	--
Cash and short-term investments (reported)	22,672.9	26,231.9	37,494.8	52,540.0	47,892.7	49,228.5

Adjusted ratios						
Debt/EBITDA (x)	2.9	0.6	0.2	--	--	--
FFO/debt (%)	25.9	146.3	328.7	N.M.	N.M.	N.M.
Annual revenue growth (%)	3.0	52.0	(17.4)	22.4	15.0	15.0
EBITDA margin (%)	6.2	6.3	7.0	8.1	8.2	8.0
Return on capital (%)	26.3	33.8	34.6	36.7	31.7	31.6

All figures are adjusted by Taiwan Ratings Corp., unless stated as reported. Figures of forecast period are based on Taiwan Ratings Corp.'s base case scenario. a--Actual. e--Estimate. f--Forecast. NT$-- new Taiwan dollar. N.M.--Not meaningful.

Liquidity

The short-term rating on Wiwynn is 'twA-1'. We believe Wiwynn has exceptional liquidity to meet its needs over the 24 months ending June 2026. We estimate the company's ratio of liquidity sources to liquidity uses to be around 3.2x over the 12 months ending June 2025 and 3.5x over the subsequent 12 months. We believe that Wiwynn's liquidity sources will still exceed liquidity uses even if its EBITDA was to drop by 50%. The company has prudent risk management characterized by its sufficient cash on hand, complete hedging on foreign currency risk, and high insurance coverage on inventory.

We also believe that Wiwynn has strong banking relationships and a generally satisfactory standing in credit markets. Wiwynn's debt carries no financial covenants.

Principal liquidity sources:

- Cash and short-term investments of NT$25.7 billion as of the end of June 2024.
- Funds from operations of NT$15 billion-NT$20 billion in 2024 and NT$20 billion-NT$25 billion in 2025.
- The issuance of offshore convertible bonds with total proceeds of around NT$19.4 billion in July 2024.
- The issuance of global depositary receipts with net proceeds of around NT$27.3 billion in July 2024.

Principal liquidity uses:

- Debt maturities of NT$3.5 billion-NT$4.0 billion over the 12 months ending June 2025, and NT$4.0 billion-NT$4.5 billion over the subsequent 12 months ending June 2026.
- Working capital outflow of NT$10 billion-NT$13 billion over the upcoming 12 months ending June 2025, and NT$5 billion-NT$8 billion over the subsequent 12 months ending June 2026.
- Capex of NT$5.0 billion-NT$5.5 billion in 2024 and NT$3.5 billion-NT$4.0 billion in 2025.
- Cash dividend payout of 60%-65% of the previous year's net income in 2024-2025.

Ratings Score Snapshot

Wiwynn Corp.		
	To	**From**
Issuer Credit Rating	twA/Stable/twA-1	twA/Stable/twA-1
Business risk	Fair	Fair
Country risk	Moderately high	Moderately high
Industry risk	Moderately high	Moderately high
Competitive position	Fair	Fair
Financial risk	Modest	Modest
Cash flow/Leverage	Modest	Modest
Anchor	twa+	twa+
Modifiers		
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	Exceptional (no impact)	Adequate (no impact)
Management and governance	Neutral (no impact)	Neutral (no impact)
Comparable ratings analysis	Negative (-1 notch)	Negative (-1 notch)
Stand-alone credit profile (SACP)	twa	twa
• Entity status within group: Highly strategic • We assess Wiwynn as an insulated and highly strategic subsidiary of Wistron group. The issuer credit rating on Wiwynn can be one notch above the parent group credit profile on S&P Global Ratings' global rating scale if Wiwynn's stand-alone credit profile is one or more notches higher than the group credit profile.		
Note: The descriptors are on a global scale.		

Related Criteria & Research

Related Criteria

- Criteria | Corporates | General: Sector-Specific Corporate Methodology - April 04, 2024
- 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
- 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
- General Criteria: Principles Of Credit Ratings - February 16, 2011

Related Research

- Taiwan Ratings' Ratings Definitions – November 11, 2021

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

Ratings List

Ratings Affirmed

Wiwynn Corp.	
Issuer Credit Rating	twA/Stable/twA-1

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.