Bulletin

New Aircraft Procurement To Squeeze China Airlines' Financial Buffer

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China Airlines Ltd. (twA-/Stable/twA-2) has announced an order for multiple new aircraft that is beyond our original forecast. This could squeeze the company's financial buffer over the delivery period which starts in 2029.

This round of aircraft procurement includes 20 passenger planes and 4 freighters with a total sum of no more than US$11.9 billion or about new Taiwan dollar (NT$) 385 billion. Although the delivery timetable and final amount are subject to confirmation, we believe China Airlines' ratio of funds from operations (FFO) to debt will drop to close to 20% in 2029, which is our downside rating trigger. We base this on the carrier's procurement budget and its forecast annual FFO of NT$35 billion-NT$45 billion over the delivery period. We believe the company has insufficient time to strengthen its financial buffer before 2029. That's because the carrier already has planned capital expenditure of NT$125 billion-NT$135 billion for fleet renewal in 2025-2028.

Nonetheless, we expect the airline to improve its operating performance over the next few years which should keep our issuer credit ratings on the company unchanged over the same period. This includes higher operating efficiency due to the reduced fuel requirement of new aircraft as well as profit increases from network adjustments. In addition, strong outbound travel demand and comparatively lower capacity increases on the routes where China Airlines operates are likely to remain unchanged over the next two years. These could support the carrier's passenger yield and cargo yield to remain above the level before 2019.