

**Lianhe Global has affirmed ‘BB+’ the global scale Long-term Issuer and Issuance Credit Rating to E-House (China) Enterprise Holdings Limited; Issuer Rating Outlook Revised to Negative**

HONG KONG, 03 September 2020 – Lianhe Ratings Global Limited (“Lianhe Global”), an international credit rating company, has affirmed ‘BB+’ global scale Long-term Issuer Credit Rating to E-House (China) Enterprise Holdings Limited (02048.HK) (“E-House” or “the company”). The Outlook is revised to Negative from Stable.

Lianhe Global has also affirmed ‘BB+’ global scale Long-term Issuance Credit Rating to the USD300 million 7.625% senior unsecured USD notes due 2022 issued by E-House at the same time.

The Issuer Rating affirmation reflects E-House’s decent property pipelines and market position in its real estate agency services segment, close business relationships with top Chinese property developers and the growth prospect of its real estate brokerage network services segment.

The Negative Outlook on E-House’s rating reflects our expectation that E-House’s operating performance would be negatively impacted in 2020 from the risks and uncertainty associated with the COVID-19 outbreak on the China property market, coupled with the significant increase in debt level at end-2019, resulting in financial leverage to peak in the next 12-18 months. We would consider revising the Rating Outlook to Stable when there is a clear sign of recovery on E-House operating performance and demonstrated effort to sustainably manage its growth trajectory and financial leverage level.

**Key Rating Rationales**

***Partnership with Leading Property Developers Continues to Provide Decent Pipelines but Negatively Impacted by COVID-19 Outbreak:*** E-House has formed partnerships with many leading Chinese property developers to gain access to their portfolios of development projects to support its real estate agency services. E-House’s city coverage expanded a total GFA of signed and unsold development projects of 288.3 million square meters at end-June 2020. E-House’s has entered into strategic relationships with many leading property developers through shareholdings. The three top property developers, namely Country Garden, Vanke and Evergrande, collectively hold over 37% of shares of E-House and they are the three largest shareholders of E-House besides Mr. Zhou, the founder. With close relationships with the leading property developers, E-House has been able to continue to obtain strong pipelines of development projects to support its sales and gain market shares in the next two to three years.

However, the COVID-19 outbreak has driven down the pace of contracted sales of Chinese property developers, which experienced a significant drop in the first two months of 2020 with year-on-year decrease of c. 35.9%. With direct exposure to the transaction value of major developers, E-House's transaction value in its primary market real estate agency services and real estate brokerage network services segments has experienced a notable decrease in 1H 2020. We expect the transaction value for its primary market business to experience a year-on-year decrease of c. 20% in 2020, contributing to a lower than expected single digit growth in revenue for 2020. The growth in store network of E-House's brokerage network services business is expected to partially offset the decrease in revenue from the company's primary market real estate agency services business.

**Long Cash Conversion Cycle Puts Pressure on Liquidity:** E-House had relatively weak bargaining powers with the leading property developers in terms of collections of commission payments which resulted in cash outflow on working capital in 2018 and 2019, largely due to a substantial increase in account receivables and other receivables. The long account receivables and short account payable cycle eroded part of the operating cash flow before working capital change of E-House. Moreover, according to the agreements with leading property developers, E-House had to place, in some cases, earnest deposits with some property developers in exchange for conducting real estate agency services. These deposits are refundable once a certain time period has passed under the agreements.

As E-House has been putting more emphasis on diversifying the developer base and timely collection of commission payments, we expect the working capital requirement pressure to gradually ease. E-House's operating cash flow has turned around from an outflow of RMB244.7 million in 1H 2019 to an inflow of RMB833.2 million in 1H 2020, and we expect operating cash flow to remain positive in 2020. On the other hand, as E-House's brokerage network services business continues to grow, we expect that it will continue to put pressure on operating cash flow, partially offsetting the effect of improving working capital management, in the next 12-24 months.

**Substantial Increase in Financial Leverage:** As an asset-light company, E-House does not have any large capital expenditure plan on hand. In the past, it borrowed short-term debt mainly to support its working capital needs. In 2019, E-House made its debut in the USD bond market which lengthened its debt maturity profile while increasing its financial leverage substantially.

Financial leverage in terms of debt/EBITDA increased to c. 3.3x at end-2019 from c. 0.7x at end-2018. We expect E-House's financial leverage will peak at close to 5x at end-2020, before gradually coming down to c. 4.0x level in the next 12-24 months. As E-House continues to expand its brokerage network services and real estate agency services, we expect the company to require capital investments, with much of those covered by the proceeds from the USD note issuances and investments from Taobao China Holding Limited, an indirectly wholly-owned subsidiary of Alibaba Group Holding Limited ("Alibaba"). Therefore, we expect any subsequent debt financing will likely be for refinancing needs primarily.

### ***Co-operation with and Investment from Alibaba to Compliment Growth Trend in the Medium Term:***

On July 31, 2020, E-House entered into a share subscription agreement and a note subscription agreement with Alibaba with which Alibaba will subscribe to c. HK\$828 million worth of shares of E-House and a convertible note with a principal amount of c. HK\$1,032 million, respectively. Alibaba will hold c. 8.3% of E-House post issuance of the subscription shares and c.13.3% of E-House post conversion of the convertible note (if and when converted), surpassing Evergrande, Vanke and Country Garden as the second largest shareholder of E-House.

The co-operation with and investment from Alibaba is expected to benefit E-House through the collaboration in offline-online real estate transactions, digital marketing and post-transaction services. E-House is also expected to benefit from Alibaba's strong technological know-hows in improving the company's technology, operational efficiency and service quality. Given the time usually required to establish a co-operation and iron out a business plan, the materialization of tangible benefits from the participation of Alibaba remains to be seen and is not expected to be significant in the immediate term.

### **Rating Sensitivities**

We would consider downgrading E-House's rating if (1) its operating performance were to deteriorate as measured by an EBITDA margin to decrease to below 15% consistently, or (2) its financial leverage as measured by a debt/EBITDA ratio to increase to over 4.0x consistently, or (3) its operating performance and working capital management were to deteriorate such that its revenue experiences a material decline or operating cash flow shows sign of worsening.

An upgrade is unlikely given the negative outlook for E-House. However, if E-House's operating efficiency were to exhibit a remarkable improvement such that it could maintain a sustainable positive operating cash flow, strengthen its profitability as measured by an EBITDA margin to increase to above 35% consistently, and its financial leverage as measured by a debt/EBITDA ratio to decrease to below 2.0x consistently, we may consider upgrading E-House's rating.

### **About Lianhe Global**

Lianhe Global is an international credit rating company that provides credit ratings to corporations, banks, non-bank financial institutions, local government financing vehicles, and other asset classes around the globe. Lianhe Global also provides credit risk research and other services related to credit ratings.

### **Rating Methodology**

The principal methodology used in this E-House's rating is Lianhe Global's General Corporate Rating Criteria published on 16 July 2018 which can be found at the website [www.lhratingsglobal.com](http://www.lhratingsglobal.com).

**Note:** The above Issuer/Issuance Credit Ratings are solicited at the request of the rated entity or a related third party.

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