

Pujiang International Group Limited

Surveillance Report

Summary

Issuer Rating	BB-
Outlook	Negative
Location	China
Industry	Building Materials
Date	24 June 2022

Operating Data:

Pujiang International Group Limited	2020	2021
Revenue (RMB: in million)	1,947	2,156
Reported Gross Margin (%)	26.6	26.6
Revenue of Cables Business (RMB: in million)	1,024	1,208
Revenue of Prestressed Steel Materials Business (RMB: in million)	923	948

Source: Pujiang

Analysts

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Applicable Criteria

General Corporate Rating Criteria (31 December 2021)

Lianhe Ratings Global Limited (“Lianhe Global”) has affirmed ‘BB-’ global scale Long-term Issuer Credit Rating of Pujiang International Group Limited; Issuer Rating Outlook Revised to Negative

Summary

The Issuer Rating reflects Pujiang International Group Limited's (2060.HK) (“Pujiang” or “the company”) established track record and leading position in the bridge cables and prestressed materials markets, as well as its stable margins. We expect the company to continue maintaining its market position by successfully bidding on key projects while enhancing its profitability by improving the share of higher-margin bridge cables business's proportion in its total revenue. However, the rating is constrained by Pujiang's limited operating scale and working capital intensive business model with a weak liquidity profile.

The Negative Outlook reflects project delays primarily due to the impact of the pandemic have pushed up Pujiang's receivables and inventories in 2021, causing significant working capital outflow. Pujiang's working capital gap increased. This situation could continue in 2022, and the project delays could also affect Pujiang's revenue recognition and dampen its growth momentum.

Rating Rationale

Leading Bridge Cables Manufacturer with Advanced Techniques: Pujiang is a leading bridge cables manufacturer in China. The company can produce cables for the world's largest super-long-span bridge with the latest bridge design technical standards. Pujiang provided bridge cables for a series of Chinese and overseas landmark projects such as the Guangdong Humen No.2 bridge, the second-largest super-long-span suspension bridge in China, and the 1915 Canakkale Bridge in Turkey, the largest super-long-span suspension bridge in the world. We expect Pujiang to maintain its leading market position due to the bridge cables industry's high entry barriers and Pujiang's operating track record as well as its ongoing effort in research and development.

Continuous Improvement in Operating Scale and Profitability: Pujiang's operating scale has grown constantly in the past five years. Its total revenue increased by 10.7% year-on-year to RMB2,176 million in 2021, mainly driven by the growth of its bridge cables business, which increased by 18% year-on-year to RMB1,208 million, accounting for 56% of the company's total revenue in 2021. The company also has good project pipelines containing 90 ongoing projects, and the outstanding contract value amounted to c. RMB1,353 million. Pujiang's revenue from prestressed materials increased by 2.7% year-on-year to RMB948 million in 2021, accounting for 44% of its total revenue. As Pujiang's new facility in Jiangxi Province's Jiujiang city is expected to be put into production in the second half of 2022, we expect prestressed materials' revenue to grow steadily in 2023 and 2024.

Pujiang's reported gross margin was stable at the 25%-27% level in the past three years. For the bridge cable business, the company locks in its margin by sourcing procurement based on the contract value of the won projects to ensure it can maintain a c.35% gross margin for this segment. Pujiang usually prices its prestressed materials product on a cost plus a fixed margin (15%-17%) basis. The higher-margin bridge cables business's share in Pujiang's total revenue showed an increasing trend, which was c.49%, 53% and 56% in

2019, 2020 and 2021, respectively. We expect Pujiang's reported gross margin to gradually increase in small increments.

Large-scale Infrastructure Investments Support Pujiang's Growth in the Medium Term, But the Pandemic Variant Brings Uncertainty: The Chinese government is accelerating infrastructure investment to boost economic growth. According to the Ministry of Transport of China ("MOT"), the fixed asset investments in road construction increased by 11.8% year-on-year in the first quarter of 2022. We expect a number of bridge projects to be opened for tender in 2022 and 2023, and Pujiang has a good chance to win a part of them, given the required technology and specifications. This could fuel Pujiang's growth in the medium term.

However, the pandemic induced restrictions could delay the projects' schedule. MOT's statistics suggested that fixed asset investments in road construction decreased by 0.4% year-on-year in April 2022. We expect Pujiang's revenue growth to be moderate in 2022. If the situation lasted for a prolonged period, Pujiang's growth momentum could be further hindered.

Tight Liquidity and Increasing Financial Leverage: Pujiang's liquidity remained tight. The company had total cash on hand of RMB608 million (unrestricted cash of RMB373 million) at end-2021, compared to its short-term debt of RMB1,921 million. This is mainly due to the working capital-intensive nature of Pujiang's business model. The company needs to prepay its suppliers and provide deposit guarantees for its projects. In addition, the pandemic caused some project delays in 2021, resulting in the increase in receivables and inventories, thus leading to a substantial operating cash outflow of RMB652 million in 2021 (2020: inflow of RMB111 million). Despite the fact that we expect Pujiang to be able to roll over its short-term borrowings based on the established relationship with its key borrowing banks, the company's liquidity buffer has been significantly reduced, which increases the uncertainty on its ability to cope with potential shocks should operating or financing environment turn undesirable.

Pujiang's reported debt increased significantly to RMB2,019 million at end-2021 from RMB1,640 million at end-2020, representing year-on-year growth of 36%, with short-term debt accounting for c. 95% of the total debt. Its financial leverage, as measured by adjusted gross debt/capitalization, increased to 48.7% at end-2021 from 44.1% at end-2020. Considering the potential project delays in 2022 and Pujiang's increasing operating scale, the company may face operating cash outflow persistently in the next 12-18 months. We expect Pujiang's financial leverage, as measured by adjusted gross debt/capitalization, to reach c.50%-52% between 2022 to 2024.

Rating Sensitivities

We would consider downgrading Pujiang's rating if (1) its liquidity profile were worsened and/or its operating performance in terms of revenue, margin and cash flow generation were to deteriorate significantly, and/or (2) it were to increase its financial leverage as measured by its EBITDA interest coverage consistently below 2.0x or debt over EBITDA leverage consistently above 5.5x.

An upgrade is unlikely given the negative outlook on Pujiang. However, if Pujiang were able to improve its working capital and liquidity profile, we would consider revising the outlook to stable.

Company Profile

Pujiang is a manufacturer and seller of long-span bridge cables and prestressed steel materials in China. It was first established as a state and collective jointly-owned enterprise named Shanghai Pujiang Cable Factory in 1989. It was then converted into a joint stock company and renamed as Shanghai Pujiang Cable Co., Ltd. (“Shanghai Pujiang”) in 2001. The company has been listed on the Hong Kong Stock Exchange since 28 May 2019.

On 17 December 2020, Pujiang announced the proposed privatization of Ossen Innovation Co., Ltd. (“Ossen Innovation”), a subsidiary mainly engaged in the prestressed materials business. Ossen Innovation’s ADSs were listed on NASDAQ (stock code: OSN). The company indirectly held approximately 65.9% of the issued share capital of Ossen Innovation as of 17 December 2020. The privatization was intended to improve Pujiang’s upstream and downstream business integration capabilities.

On 7 September 2021, Pujiang announced that the privatization was completed, and Ossen Innovation became a wholly-owned subsidiary of the company.

Pujiang is committed to consolidate its leading position in the bridge cable manufacturing and prestressed material market by continuously improving the production capacity and operation efficiency. Among them, the high-tech galvanized production line and the new plant of Jiujiang factory will be completed in the second half of 2022, increasing its capacity reserves and production lines. In order to enhance the research and development capabilities, Pujiang’s new research and development center will also be completed in the second half of 2022.

Pujiang’s Shareholding Structure at end-2021

Shareholder	Percentage
Elegant Kindness (100% owned by Mr. Tang Liang)	68.22%
China Silver Asset Management Limited	9.77%
Others	22.01
Total	100.0%

Source: Pujiang’s 2021 annual report

Key Financial Assumptions

- Revenue growth: 4% to 25% for 2022-2024
- Reported gross margin: 26% to 28% for 2022-2024
- New awarded bridge cables contact value: RMB1,300-1,700 million per year

Key Financial Metrics

2020A-2024F	Debt/EBITDA	EBITDA/Interest	Debt/Capitalization	Quick Ratio
Weighted Average	5.7x	3.2x	50.4%	0.7x

Source: Pujiang’s annual reports and Lianhe Global’s adjustments and forecasts

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