



# E-House (China) Enterprise Holdings Limited (“E-House”)

## Initial Issuer Report

### Summary

Issuer Rating	BB+
Outlook	Stable
Location	China
Industry	Real Estate Service
Date	19 December 2019

**Lianhe Ratings Global Limited (“Lianhe Global”) has assigned a ‘BB+’ global scale Long-term Issuer Credit Rating to E-House (China) Enterprise Holdings Limited. The Outlook is Stable.**

### Summary

The Issuer Rating reflects E-House (China) Enterprise Holdings Limited (“E-House” or “the company”)’s low financial leverage, strong pipelines of development project listings, and close alliance with many leading Chinese property developers as its strategic shareholders.

The Stable Outlook of E-House’s rating reflects our expectation that E-House would maintain a sustainable revenue growth from its real estate agency services while its revenue from brokerage service networks would likely enjoy a rapid growth upon its complete implementation of platform and intake of independent brokers into its brokerage networks.

We also expect that the Shanghai-based company currently low financial leverage will likely increase. We believe that, as E-House expands its business, it is likely to incur more debt in the following 12 to 24 months. Rating constraints include its limited market share in a fragmented real estate agency market and a long cash conversion cycle.

### Operating Data:

E-House (China) Enterprise Holdings Limited

	31 Dec 2017	31 Dec 2018
Revenue (RMB: in million)	4,633	5,948
GFA* of Sellable Resources (million square meters)	205.8	281.8
Revenue per employee (RMB: in thousand)	N/A	245.6

Note:  
GFA: Gross floor area  
Source: E-House’s 2017-2018 annual reports and Lianhe Global

### Rating Rationale

**Strong Partnerships with Leading Property Developers Enhanced Pipelines:** E-House has formed strategic alliances 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 coverage expanded to 204 cities with a total GFA of signed and unsold development projects at about 281.8 million square meters at end-2018 (end-June 2019: 282.8 million square meters).

E-House has entered into strategic cooperation with many leading property developers. The top three Chinese property developers in the market, namely Country Garden, Vanke and Evergrande, each held about 11.68% shares of E-House at end-June 2019. The company enlisted a total of 27 leading property developers as its shareholders at the time of its IPO in July 2018. With those close relationships and affinity to the leading property developers, E-House is able to obtain strong pipelines of development projects to support its sales and gain market shares in the next 2-3 years.

**Long Cash Conversion Cycle Caused by Limited Bargaining Power:** E-House’s moderate market position limits its bargaining power with the leading property developers in terms of commission collections, which rendered the relatively long collection time of account receivables due from the leading developers. The relatively long days of account receivables and the short days of account payables eroded the liquidity profile of E-House and caused a negative cash flow on working capital in 2018.

The company from time to time needs to place earnest deposits to property developers in exchange for exclusive consignment of certain flagship projects. Albeit these deposits are refundable when E-House fulfils its duties and discharges itself from the service agreements, the sizeable cash deposits also weigh on its short-term operating cash flow. As E-House’s real estate

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### Applicable Criteria

General Corporate Rating Criteria (16 July 2018)

brokerage network service business grows, we expect that its operating cash flow will continue to be under pressure in the following 12-24 months provided its current standard operation procedures continue.

**Financial Leverage Expected to Rise from Low Base:** We expect E-House's financial leverage will gradually increase in the next 12 to 24 months as it rapidly expands its brokerage networks and real estate agency services, which incur more long-term borrowings to fund such capital investments. Before 2018, E-House did not have any long-term debt nor any large expenditure plan. As an asset-light property brokerage firm, E-House inherently utilized trivial leverage and only borrowed short-term debt mainly to support its working capital needs. Its financial leverage ratio from 2016 to 2018 was low as measured by a debt over EBITDA ratio at below 1.0x.

### Rating Sensitivities

We would consider downgrading E-House's rating if its operating performance were to deteriorate as measured by an EBITDA margin to decrease to 15% or its financial leverage were to increase as measured by a debt/EBITDA ratio to above 4.0x.

We would consider upgrading E-House's rating if its financial performance were to exhibit a remarkable improvement in terms of maintaining a sustainable positive operating cash flow, increasing profitability as measured by an EBITDA margin to increase to above 35%, and strengthening market position/share.

### Company Profile

E-House, formerly known as E-House (China) Holdings ("E-House Holdings"), started its real estate agency business in 2000. E-House Holdings was listed on the NYSE in 2007 and then privatized in late 2016 for the reorganization of its businesses and ownership. The company was listed on HKEX in 2018, controlled by Chairman Mr. Zhou Xin who owned 20.9% of the company as the single largest shareholder at end-June 2019 through several intermediate companies.

E-House is one of the leading primary market real estate brokers in mainland China with a focus on projects developed by major property developers. In addition to the brokerage services which contributed about 80.0% of the company's total revenue in 2018, E-House also provides industry data and consulting services (13.0%), as well as real estate brokerage network services (7.0%) to small-and-medium-sized brokerage firms. (EXHIBIT1)

The company has teamed up with top property developers in the market as strategic partners to strengthen its brokerage pipelines, especially the flagship ones that attract buyers. E-House held 282.8 million square meters of signed and unsold reserve projects by end-June 2019, up from 206.0 million square meters at end-2018.

**Exhibit 1: E-House's Revenue Breakdown by Business Segment (RMB: in million)**

Revenue/ % of total	FY2016		FY2017		FY2018		1H2019	
Real estate agency services in the primary market	3,569	89.3%	3,927	84.7%	4,753	80.0%	2,577	59.5%
Real estate data and consulting services	396	9.9%	629	13.6%	773	13.0%	443	10.2%
Real estate brokerage network services	31	0.8%	77	1.7%	421	7.0%	1,310	30.3%
<b>Total</b>	<b>3,996</b>	<b>100%</b>	<b>4,633</b>	<b>100%</b>	<b>5,948</b>	<b>100%</b>	<b>4,330</b>	<b>100%</b>

*Source: E-House's 2016-1H2019 annual and interim reports*

## Business Profile

### Moderate Market Position

The fragmented and overly competitive real estate agency market mainly consists of primary (newly-completed properties) agency and secondary (pre-owned properties) agency markets, with numerous firms providing similar services on price-cutting strategies. Due to low entry barriers, the penetration rate of primary agency market decreased over the past years as the number of service providers increased; the top 10 real estate agencies' total market share edged down to 14.1% in 2018 from 17.1% in 2015, according to a third-party report.

According to another third-party research, E-House was among one of the top 5 property brokers in the Chinese market with about 4-5% market share of total primary residential transaction amount. However, due to its lack of bargaining power in the competitive market, the average commission rate stayed stable at about 0.9% on the amount of sales while its market position in terms of total GFA of new properties sold increased to 41.3 million square meters from 26.1 during 2015 to 2018. (EXHIBIT 2)

We see E-House's primary agency service pipeline being more secured than the other similarly-sized real estate agencies given the leading property developers' material shareholding in the company and its strategic alliances with other major market players. Such arrangements give E-House strong information access to the projects before they are released to the market and support its business development in the primary market for the next 2 to 3 years.

E-House has put efforts on decreasing its revenue concentration on projects of single property developer by building more partnerships with other property developers. The agency sales contribution from Evergrande was 37% in 2018 and 39% in 2017, respectively.

**Exhibit 2: E-House's GFA of Properties Sold, Contracted Pipeline, and Commission**

Amount / Ranking	FY2015	FY2016	FY2017	FY2018
Total GFA of new properties sold (million square meters)	26.1	35.5	37.2	41.3
Total value of new properties sold (RMB million)	267,468	406,078	432,982	531,454
Total GFA of contracted pipeline properties (million square meters)	160.7	165.4	206.0	281.8
Average commission rate (%)	0.87	0.88	0.91	0.89

Source: Company

### Moderate Business Diversity

The company defines Chinese property developers as its main clientele. The top 5 revenue contributors are all property developers whose businesses with E-House accounted for about 43.7% of its total revenue in 2018. Albeit the management has enacted measures to ease this earnings concentration by partnering with more developers and establishing the new platform of brokerage networks, we expect E-house's profitability to stay reliant on these shareholders and susceptible to the same headwinds that also affect the whole property developer sector, including home price gyration, regulatory changes, and macro-economic outlook.

E-House's suppliers were labour dispatch agencies, office space providers, renovation service providers, advertising companies, and real estate brokerage firms. The top 5 suppliers accounted for less than 10% total purchases of E-House. We see no material concentration risks in the vendor profile.

## Financial Profile

### Key Assumptions

- Revenue: RMB10.4-12.5 billion for 2020-2021
- Sell through rate: 55-60% for 2020-2021
- Average Commission Rate: 0.8-1.0% for 2020-2021

### Key Financial Metrics

2017A-2021F	Debt/EBITDA	EBITDA/Interest	Debt/Capitalisation	Quick Ratio
Weighted Average	2.04x	14.30x	30.96%	1.77x

Source: E-House's 2017-2018 annual reports and Lianhe Global's adjustments and forecasts

### Brokerage Network Business to Drive Revenue

We expect that income from E-House's brokerage network services will be the profitability driver when the community platform and the members of independent brokers within this network achieves a critical mass in the next 1 to 3 years. This will complement the company's current service offering, expand its client acquisition nodes into new cities and help mitigate associated risks of revenue concentration in the real estate agency businesses.

Its EBITDA margin has experienced strong growth to 24.1% in 2016 from 16.7% of the previous year but only posted slight enhancement since then (2017: 25.0%; 2018: 28.5%). The growth of E-House's real estate agency services in the primary market, and real estate data and consulting services will remain stable in our financial projection for 2019-2021. Signed pipeline portfolio with the large property developers will continue to support the revenue growth but the commission rate for real estate agency services will stay flat at 0.8% range given the fierce market competition.

Synergic effects between E-House's brokerage business line and real estate data and consulting services are material in our view. As the company's current client coverage of the latter segment have included almost all industry participants, the gathered information provides the management solid analysis for the continued business development of property brokerage services. However, the growth of the data business line will be stable and the increment will be of the value-added services requested by the current customers or provided by E-House.

### Leverage Expected to Increase from Low Base for Business Expansion

E-House's debt level is likely to increase in 2019 and 2020 from the low base at end-2018 as part of its plan to expand the operation, especially the brokerage network service business that requires large cash endowment. The company issued USD notes through its offshore USD bond channel in 2019, which will likely boost its financial leverage in terms of debt over EBITDA to 2.8x at end-2019 from 1.0x at end-2018. We project that E-House's debt increase in 2020 and 2021 will mainly result from its growing operating needs.

## Liquidity

### Liquidity Profile Constrains Credit Profile

Substantial increase of receivables in E-House's book highlights its limited bargaining powers with the developers, pressuring its cash conversion cycles and eclipsing the net operating cash flow to a negative amount on top of the company's growing commission advances extended to the independent partner brokers.

In general, there is a grace period of up to 3 months for the company to receive commission payments from property developers after they have collected cash of contracted sales from homebuyers, whilst E-House prepays commissions to the network brokerage firms it works with. Its account receivables at end-2018 doubled that of end-2017.

Moreover, the business arrangements often dictate brokerage firms like E-House to provide refundable earnest deposits to property developers in exchange of the rights to represent certain flagship projects. These deposits also put pressure on its short-term operating cash flow at end-2018. With the company's plan to grow its brokerage network services business, its operating cash flow will continue to be under pressure.

E-House passed the liquidity test for the next 12 months provided its cash of RMB3.0 billion on hand was ample to cover its RMB1.3 billion short-term debt at end-June 2019 and our assessment of its stable access to various financing channels both in the onshore and offshore markets.

### Appendix I: E-House's Rating Factor

Rating Factors	Weight	Initial Rating
<b>I. Market Demand Analysis</b>	<b>15.0%</b>	<b>bbb</b>
<b>II. Business Analysis<sup>1</sup></b>	<b>45.0%</b>	<b>b+</b>
<b>III. Financial Analysis<sup>2</sup></b>	<b>40.0%</b>	<b>a+</b>
<b>IV. Base Score</b>	<b>100.0%</b>	<b>bbb-</b>
<b>V. Industry Risk</b>		<b>bb</b>
<b>VI. Qualifiers</b>		
Liquidity		Neutral
Corporate Governance		Neutral
Debt Structure and Financial Policy		Neutral
Idiosyncratic Analysis		Neutral
<b>Stand-Alone Creditworthiness (SAC)</b>		<b>bb+</b>
<b>VII. External Support</b>		
Corporate Entity Support		Nil
<b>Issuer Credit Rating</b>		<b>BB+</b>

Source: Lianhe Global

<sup>1</sup> Business Analysis contains sub-factors of market position, diversification, competitive position, operating efficiency and profitability.

<sup>2</sup> Financial Analysis contains sub-factors of debt/land bank, EBITDA interest coverage, debt/capitalization and quick ratio.



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