

## CMBI Credit Commentary - HONHUA

### **HONHUA: Buy at cash price 88/90 irrespective of its major ownership under CASIC or Dongfang Electric**

Honghua Group announced its largest shareholder China Aerospace Science and Industry (CASIC) has entered into gratuitous transfer agreement to transfer its entire stake (29.8%) in Honghua Group to Dongfang Electric International Investment Co. Ltd for nil consideration, subject to SASAC's approval.

Dongfang Electric International Investment Co. Ltd is a wholly owned subsidiary of Dongfang Electric Corporation, which is a Central SOE 100% owned by SASAC focused in power equipment manufacturing. We view this share transfer to Dongfang Electric is to align their respective business operations. Honghua's oil servicing equipment business is more synergetic with Dongfang Electric's power equipment operation, than with CASIC's.

Repayment acceleration of the notes will only be triggered upon a Change of Control, and a rating decline, per HONHUA's USD bond OC.

**We have seen some sign of weakening support from CASIC prior to this stake transfer proposal.** Last week, a CASIC associate company - Jiangsu Hongjieding (46.2% owned by CASIC, and 53.8% owned by Honghua's vice chairman Zhang Mi) defaulted on a legacy inter-company loan to Honghua (RMB 630 million payable by 31 Dec 2021) which will bring a non-cash loss of RMB300mn-400mn to Honghua.

**Nonetheless, CASIC is the keepwell provider to HONHUA 6.375 '22 notes.** We understand CASIC intends to maintain the keepwell. Under its keepwell letter in the USD bond OC, a) CASIC intends to own no less than 25% stake of Honghua Group. In addition, b) CASIC intends to cause Honghua Group to have sufficient liquidity to ensure timely payment of the USD notes. In an event if this stake transfer does not go through, we expect CASIC will provide liquidity support to Honghua's USD bond repayment, given CASIC consolidates Honghua's financials.

**Given both CASIC and Dongfang Electric are Central SOE 100% owned by SASAC, we expect Honghua can tap on new bank lines or future USD bond issuance to repay its HONHUA 6.375 '22 notes in Aug 2022, irrespective of its major ownership under CASIC or Dongfang Electric. We suggest a tactical Buy on HONHUA 6.375 '22 at cash price 88/90.**

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