

CMBI Credit Commentary**CHFOTN – Next catalysts**

Background - A China Fortune Land issued onshore corporate bond 17Xingfu-MTN001 was sold at 80.0 (YTM 23.4%, trade size RMB25mm) on 7 December, this represented a 16 points deviation from the value estimated by Shanghai Clearing House on its respective bond. The onshore trade subsequently triggered a sell-off in offshore USD bonds with front-end bonds dropping 3-4pts and long-end bonds dropping 6-8pts. The unexpected onshore trade was triggered by forced redemption on a fixed maturity fund during a time of thin liquidity in the onshore credit bond market. **In our view, the current sell off represents fragile investor confidence on the company's deteriorating fundamentals.**

What is our view?

- **China Fortune Land (CHFOTN)'s liquidity is enough to cover its onshore & offshore bond maturities (including bonds with put options), after it draws down the perpetual bonds issued to several financial institutions this year.** As of 3Q'20, CHFOTN owns cash and equivalents of ~RMB38.6bn, as disclosed by the company's IR. By year-end, they will draw down perpetual bonds issued across the year, including RMB12bn from Ping An (through 3 various entities), RMB2bn from Western Trust, and RMB1.5bn from Zhongrong Trust. We believe this is a meaningful liquidity boost for CHFOTN and the pro-forma cash level is estimated to be over RMB50bn after the drawdown. The total maturing bonds (onshore and offshore, including puttable bonds) totals to RMB45bn in 2020 & 2021.
- **CHFOTN has ~USD400mm cash offshore, and has been working with banks since November to prepare offshore cash to redeem the CHFOTN 6.5 20 (USD920mm) and the CHFOTN 6.65 PERP (USD350mm) through its cross-border liquidity pool.**
- **CHFOTN is in progress to resell two onshore corporate bonds puttable in December, including 18Huaxia06 (RMB3bn, puttable on 20 December) and 19Jiutong05 (RMB2bn, puttable on 30 December).** The result has yet to be disclosed. We believe a substantial portion (i.e. 50%) of successful reselling would be a positive catalyst, as it would reaffirm onshore market access is still available to the company. *(Update 10/12/2020) – RMB2.982bn of the bondholders of 18Huaxia06 executed the put options as CHFOTN decided to lower current coupon rate)*

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- **CHFOTN has been keeping a close dialogue with its second largest shareholder (i.e. 25.1%) Ping An, which is fully aware of the current unfavorable market sentiment of CHFOTN.** We believe CHFOTN has strategic meaning to Ping An, given the in-depth collaboration between both parties, by carrying out the front phases of commercial property business (*please refer to the appendix - business model descriptions*). In addition, as guided, meaningful size of CHFOTN's onshore bonds are held by Ping An and its subsidiaries. We believe there is potential upside risk to the bonds if Ping An provides support through issuing perpetual bonds, anchoring a new offshore deal, assets buy-out, etc. Granting help in terms of cash flow and liquidity by Ping An could be the next major catalyst.

Appendix – CHFOTN's maturity schedule in 2020 & 2021

China Fortune Land Maturity Schedule (assuming all put options to be executed)

<i>in millions</i>	2020/09/30 RMB	Coupon	Maturity	Put-table Date	Note
Cash and Cash Equivalent	38,608.7		N/A		
Perp issued to West Trust	2,000.0		N/A	18mths after drawdown	Expect to draw down by 2020
Perp issued to Zhongrong Trust	1,500.0		N/A	18mths after drawdown	Expect to draw down by 2020
Perp issued to Pingan Trust	12,000.0		N/A	18mths after drawdown	Expect to draw down by 2020
Total Liquidity	54,108.7				
18 Huaxia Note 06	3,000.0	7.000%	2023/12/20	2020/12/20	Next put in 2022/12
\$820M USD 6.50% Senior Notes Due 2020	5,412.0	6.500%	2020/12/21		
\$350M USD 6.65 Perp Callable 2020/12/20	2,310.0				
19 Jiutong 05	2,000.0	6.950%	2024/12/29	2020/12/30	Put-table every year
2020 Total Bond Maturity & Put	12,722.0				
16 Huaxia Debt	1,500.0	4.880%	2023/1/20	2021/1/20	
\$530M USD 8.625% Senior Notes Due 2021	3,498.0	8.625%	2021/2/28		
16 Huaxia Note 02	2,000.0	7.000%	2021/3/3		
16 Huaxia Note 01	2,800.0	7.400%	2021/3/8		
16 Huaxia Note 04	3,000.0	7.400%	2021/3/24		
19 Huaxia Note 01	1,000.0	5.500%	2024/3/25	2021/3/25	Next put in 2023/03
16 Huaxia Note 05	2,000.0	7.200%	2021/4/18		
16 Huaxia Note 06	4,000.0	7.200%	2021/5/12		
18 Huaxia Note 02	525.0	6.800%	2023/5/30	2021/5/30	
18 Jiutong 02	1,400.0	5.900%	2021/6/1		
18 Jiutong 03	910.0	7.400%	2021/6/11		
18 Huaxia Note 03	2,000.0	4.400%	2022/6/20	2021/6/20	
\$200M USD 9.00% Senior Notes Due 2021	1,320.0	9.000%	2021/6/21		
\$940M USD 9.00% Senior Notes Due 2021	6,204.0	9.000%	2021/7/31		
17 Jiutong Private Note 01	1,000.0	6.200%	2021/8/17		
2021 Total Bond Maturity & Put	33,157.0				

Appendix - business model description

CHFOTN is not only the largest industrial park developer in China, but also a top-20 residential property company. It is now turning into a commercial property manager/constructor, as part of cooperation with Ping An.

Industrial park business

CHFOTN is the largest industrial park developer in China with a history of more than 20 years with footprints in Pan-Beijing Area, Yangtze Delta Area, Great Bay Area, etc. It maintains strong relationships, and has developed expertise working with local government in the Pan-Beijing Area through PPPs, and is

trying to duplicate the high-margin business to other regions (e.g. Jiashan, Lishui, etc.). Based on our communication with the local management team, we understand the industrial park model can be illustrated as the below few steps,

- a. Local government (normally district/county level and close to tier 1-2 cities such as Beijing, Nanjing, etc.) mandates CHFOTN to develop industrial park through PPP agreement. Such level of government usually has weaker bargaining power than CHFOTN as it counts on CHFOTN for infrastructure development and referral of investment and the up-front investment for local government is small.
- b. CHFOTN sets up operating company and cooperate with local government on decision-making process.
- c. CHFOTN designs and plans the industrial park, then consolidates the land, constructs the infrastructure and develops the industry and solicits investment (such as NEV, auto parts, food & beverage, etc.). CHFOTN also sets investment rules. The Lishui (麗水) project demonstrates one such example. CHFOTN requires that first year (2016) investment not exceed RMB400mm, annual cash flow breakeven at the 3rd year (2018), and project cash flow breakeven at the 5th year (2020).
- d. While the front stages of the industrial park model (design, land consolidation and infrastructure construction) are cash consuming (CHFOTN only charges local government for 15% of the development costs), the later stage (investment referral) is highly profitable. CHFOTN charges local government ~45% of the investment it solicits to the industrial park as referral fees. This part of the business contributed to 50% of CHFOTN's gross profit.

Residential property business

CHFOTN develops residential property in satellite cities (mainly tier 3-4) around the industrial park and enjoys economical land costs (avg. land costs 3.5k/sqm vs. ASP 9k/sqm) and less land reserve needs thanks to 1) its tight relationship with local government from the industrial park business; 2) less competition in land auctions. As of 2019, the company has 10.6mm sqm undeveloped land, while the GFA sold in 2019 was 11.8mm sqm. The insufficient land reserve is mainly due to the conservative land acquisition in 2018/2019. However, we believe shortages in its land bank is mitigated by the aggressive land investment in 2020 (RMB32.3bn as of 1H'20 vs. RMB18.1bn as of 2019).

Commercial property business

On top of traditional industrial park and property development business, Fortune Land has adopted its new asset-light business (Investment property) with the expectation of synergy with Ping An. Under such scheme, Fortune Land acquires the IP assets at the initial phase, restructures the land license and sells the projects at cost to Ping An (as Ping An is not allowed to obtain residential land by regulator). Fortune Land will continue to develop and manage the project after the asset disposal and charges Ping An for construction and management fees in the 2nd and 3rd phase. Such transaction requires Fortune Land to hold the IP on behalf of Ping An for 6-12 month, which adds additional pressure on its balance sheet.

In Aug'19, Ping An acquired Beijing Fengtai project from Fortune Land at the cost of RMB5.39bn, following the pre-signed agreement. The transaction is the first collaborative deal completed, to be followed by the

Wuhan Changjiang Center project (Fortune Land acquired in 2H'19) and Nanjing project (acquired in 1H'20). Both assets are expected to be taken off balance sheet by the end of 2020 with cash inflow expected at RMB10bn, as guided by management. However, the total investment in IPs in 2020 will aggregate to RMB25bn, leading to RMB15bn free cash outflow during this segment.

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