



See the depth of credit fundamentals

—Financial performance analysis of industrial bond issuers in 2018 and Q1 2019

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Overall financial performance of issuers in the bond market

- In 2018 and Q1 2019, **total profits** of industrial bond issuers in the bond market was **growing slowly**. Overall, the **leverage was stable** at around 59%. The proportion of high-leverage (asset-liability ratio $\geq 70\%$) issuers stayed around 27%, with a little change year on year. **Total short-term debts of all market issuers have fallen from the previous year**, and over half of the issuers witnessed a YoY decline in short-term debt size. In respect of cash flow, benefiting from financing support policies, the **shortage of CFF of issuers was slightly mitigated** in Q1. In the meanwhile, profitability growth enabled **CFO to further improve**. Hence, **total cash and cash equivalents** of issuers **maintained a mild growth**. Nearly 60% of the issuers enjoyed a YoY expansion in the cash and cash equivalents. Over half of them showed enhanced capacity to pay off short-term debts with cash and cash equivalents, with **short-term solvency improving**.
- In Q1 2019, the number of new defaulters in the bond market increased significantly compared with last year. However, according to the latest financial performance mentioned above, all main financial indicators of issuers in the whole market improved to varying degrees. **The situation of increased defaults and the trend of credit fundamentals seemed against each other**. Actually, in the market environment with increasing financing support and moderate fund supply, the credit risk in the bond market tends to diverge faster. **An increase in defaults is caused by faster liquidation of a small number of issuers with high credit risk and poor risk resistance, while the short-term solvency indicators of most of the issuers in the market improved**. On the whole, **credit fundamentals of industrial bond issuers took a turn for the better**.

Financial performance of bond issuers in major industries

- Cash flow of **steel & iron and traditional energy, equipment and chemical industries** improved, with short-term debt pressure eased. Most issuers' short-term solvency in the industries was strengthened.
- More issuers of **pig farming & meat processing** and **film & TV entertainment** industries suffered a loss in net profit. Most issuers' CFO and CFF declined, and short-term debt pressure continued to mount, leading to most of the issuers' short-term solvency more weakness. Therefore, attention should be paid to their subsequent credit risk trends.
- Despite most issuers' further improvement of profitability in the **real estate industry**, it is necessary to be vigilant about future debt repayment pressure taking into consideration the rising maturity pressure of short-term debts and tight financing environment.

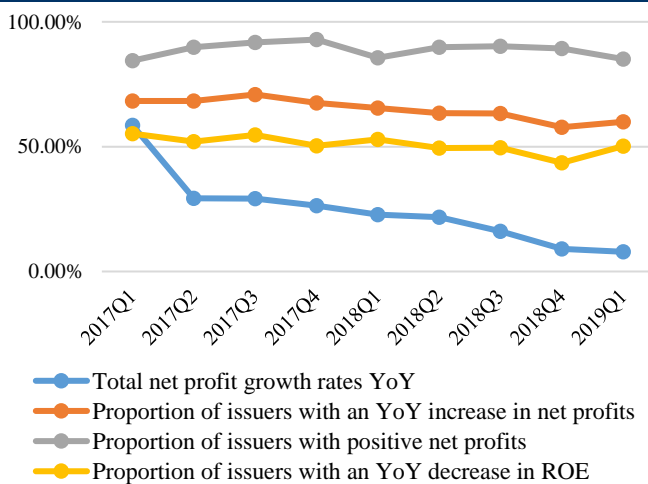
In Q1 2019, the credit exposure in the bond market increased. And compared with last year, much more new defaulters appeared. To uncover whether it implies the deterioration of overall solvency of bond market issuers, this report, which based on the sampling investigation of industrial bond issuers in the entire market and followed up with the latest financial performance of issuer samples in 2018 and Q1 2019, analyzes the changes of the credit fundamentals of industrial bond issuers from four aspects, including profitability, capital debt structure, liquidity and short-term solvency. This report also studies the latest financial performance of issuers in six major industries of steel & iron and traditional energy, equipment, chemical, pig farming & meat processing, film & TV entertainment and real estate, so as to comprehensively track the credit risk trends of major industries.

I. Overall Financial Performance of Issuers in the Bond Market

1. State of business: Profit grew slowly, and nearly 60% of issuers registered a YoY increase in net profit

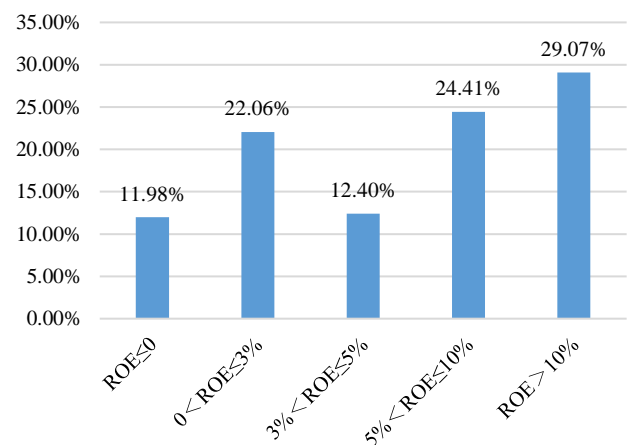
In 2018 and Q1 2019, total profits of issuers in the bond market continued to grow, however, the YoY growth slowed down further. The YoY growth rates of total net profit of 2018 and Q1 2019 were 8.99% and 7.89%, respectively, indicating a drop of more than 15 percentage points. From the perspective of the change in profits of all issuers, the proportion of issuers who made profits exceeded 85%, which was very close to that of the previous year. However, the proportion of issuers with increasing net profits slightly decreased from two-thirds to around 60%, and more than half of the issuers' ROE were decreased year on year in Q1. With respect to the ROE distribution, nearly two-thirds of issuers had a ROE above 3% in 2018, showing a slight rise over 2017, while around 30% of the issuers had a ROE above 10%, which is almost the same as the situation of 2017.

Figure 1: Issuers' profit grew slowly



Data source: CCXI

Figure 2: Nearly two-thirds of issuers had ROE above 3% in 2018



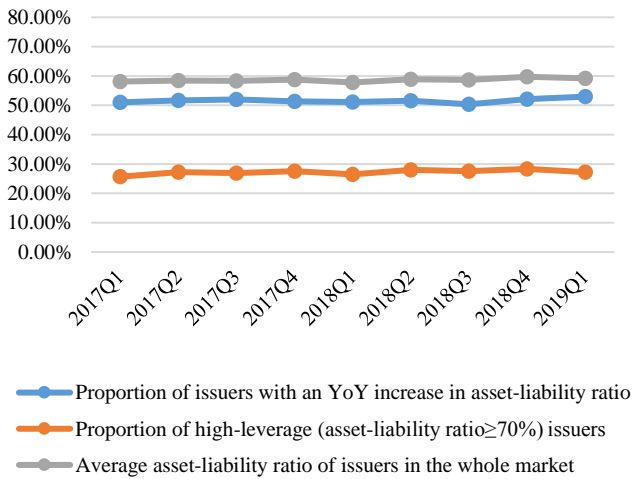
Data source: CCXI

2. Capital debt structure: Leverage was generally stable, and more than half of the issuers had less short-term debts

Leverage was generally stable. In 2018 and Q1 2019, about half of the issuers had higher leverage ratio while the others saw a decline in such ratio. By the end of Q1 2019, the average asset-liability ratio of issuers in the whole market was 59.15%, which is almost the same as the counterpart in last year, and the proportion of the issuers of high-leverage (asset-liability ratio ≥ 70%) stayed around 27%.

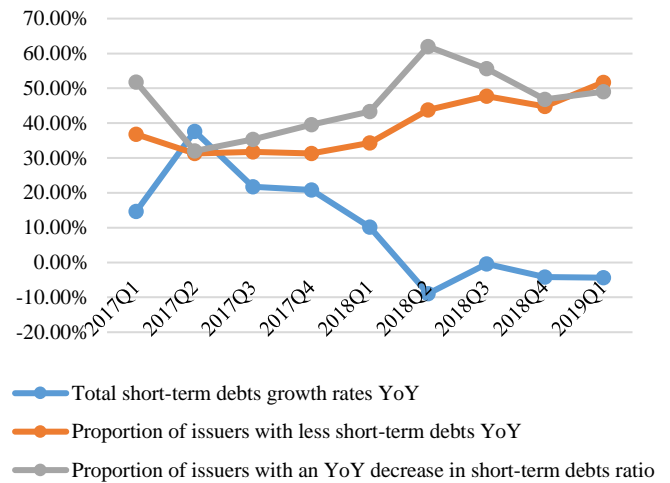
Total short-term debt continued to decrease. The total amount of short-term debt of issuers in the whole market keeps a YoY decreasing since the second quarter of 2018. By the end of 2018 and Q1 2019, total amount of short-term debt decreased by around 4% YoY and for more issuers, the burden of short-term debt have been reduced. As of Q1 2019, more than half of the issuers had less short-term debts YoY, however, the debt term structure of the whole market was not significantly improved, and issuers who have increasing amount and decreasing amount of short-term debts ratio were basically in equal portions.

Figure 3: About 50%:50% issuers increased and decreased their leverage respectively



Data source: CCXI

Figure 4: Short-term debt continued to decrease

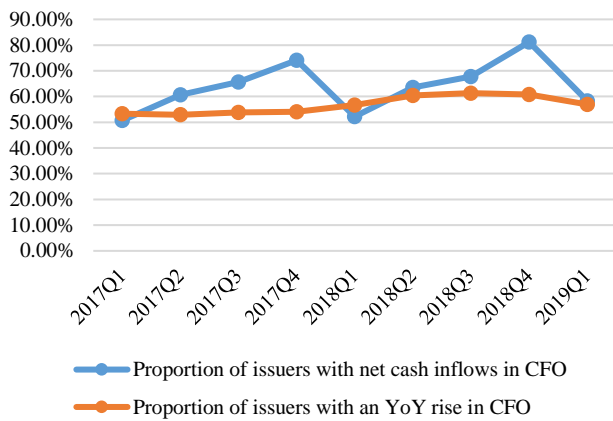


Data source: CCXI

3. Liquidity: Tension of cash flow from financing activities (CFF) eased, cash flow from operating activities (CFO) continued to improve, and cash and cash equivalents grew moderately.

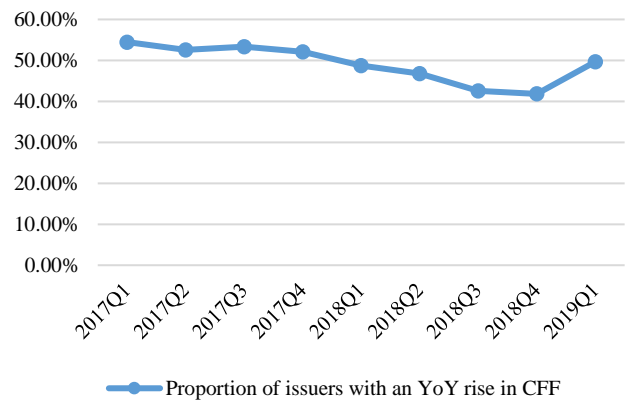
Since the second half of last year, regulators have issued policies to support the financing of private enterprises. And in this year, regulators continue to take various measures to boost the development of small and medium-sized enterprises and improve the financing environment. Such policies somewhat eased the CFF tension of issuers in this quarter. The proportion of issuers with a YoY rise in CFF rose to about 50% from only 40% in the previous year. Better profitability led to sustained CFO improvement of issuers. Specifically, in 2018 and Q1 2019, most of the issuers enjoyed net cash inflows in operating activities, and about 60% of them showed increased CFO year on year. Total amount of issuer’s cash and cash equivalents maintained a moderate growth, with the cash and cash equivalents of nearly 60% of issuers increasing YoY.

Figure 5: CFO continued to improve



Data source: CCXI

Figure 6: The tension of CFF was slightly alleviated

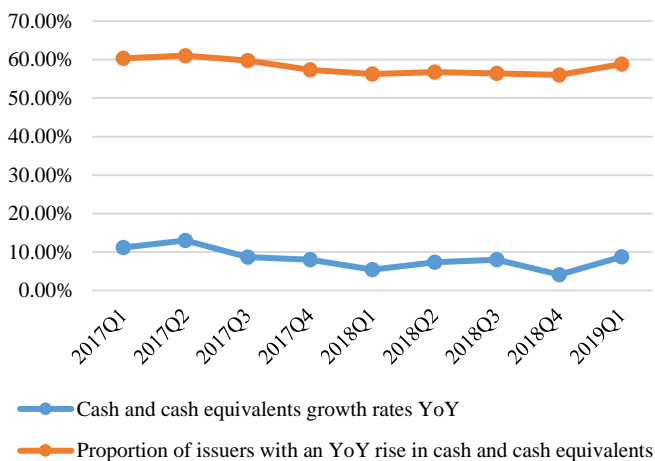


Data source: CCXI

4. Short-term solvency: Over half of issuers showed enhanced capacity to pay off short-term debts with cash and cash equivalents

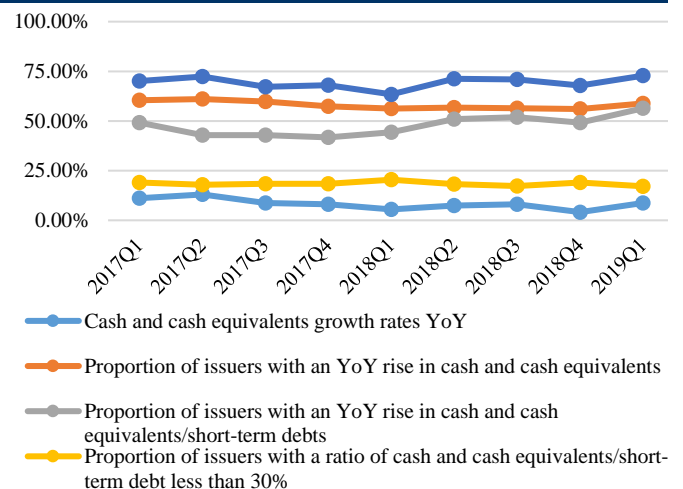
In terms of short-term solvency, as cash and cash equivalents of most of the issuers grew at a moderate rate and short-term debts continued to fall, the proportion of issuers with enhanced capacity to pay off short-term debts with cash and cash equivalents increased notably. As of the end of Q1 2019, the proportion was 56.40%, indicating a YoY rise of 12 percentage points. The median of cash and cash equivalents/short-term debts was 72.81%, up 9 percentage points YoY. The issuers with a ratio of cash and cash equivalents to short-term debt of less than 30% accounted for 17.14%, down 3 percentage points from the same period last year. Overall, the short-term solvency of bond market issuers was slightly enhanced in Q1 2019.

Figure 7: Moderate growth of cash and cash equivalents



Data source: CCXI

Figure 8: Over half of issuers showed enhanced short-term solvency



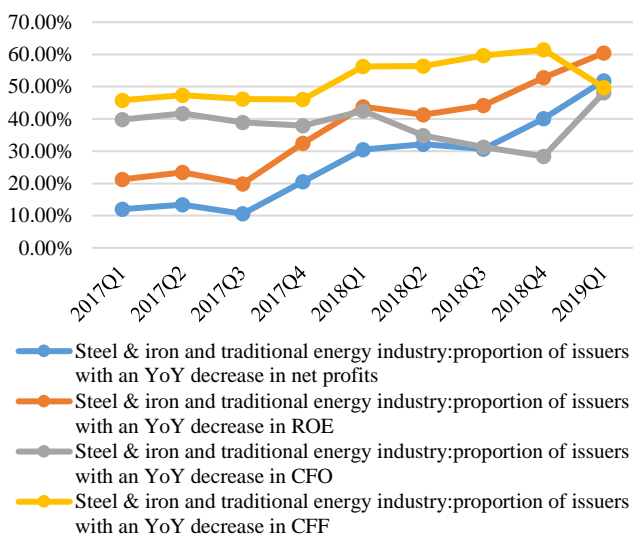
Data source: CCXI

II. Financial Performance of Bond Issuers in Major Industries

1. Steel & iron and traditional energy industry: The improvement of profitability and cash flow continued to weaken, but short-term debt pressure continued to decline and short-term solvency was further improved

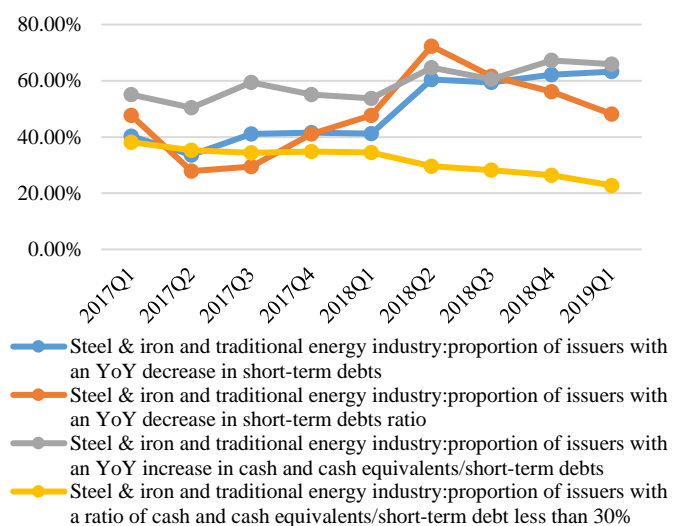
Steel & iron and traditional energy industry is very sensitive to the business cycle. Since 2018, macroeconomic growth has slowed down, and the improvement of profitability and cash flow of issuers in the industry has continued to weaken. However, benefited by the continuous decline of short-term debt pressure, the short-term solvency of most issuers in the industry has been improved to a certain extent. In terms of profit, since the second half of 2018, the proportion of issuers with declining net profit and ROE in the industry has increased significantly, which increased to more than 50% in Q1 2019. The weakening of profit improvement in the industry also adversely affected the cash flow of some issuers. In the first quarter, the proportion of issuers with deteriorating CFO increased to nearly 50%, while the CFF did not improve significantly. The overall cash flow was mediocre. However, from the perspective of short-term debt pressure, in 2018 and Q1 2019, the short-term debt of more than 60% of issuers in the industry was reduced YoY. Based on the above performance, the short-term solvency of steel & iron and traditional energy industry has been further enhanced, and about two-thirds of issuers showed enhanced capacity to pay off short-term debts with cash and cash equivalents.

Figure 9: Weaker improvement of profitability and CFO



Data source: CCXI

Figure 10: Short-term debt pressure dropped, and about two-thirds of issuers showed stronger solvency



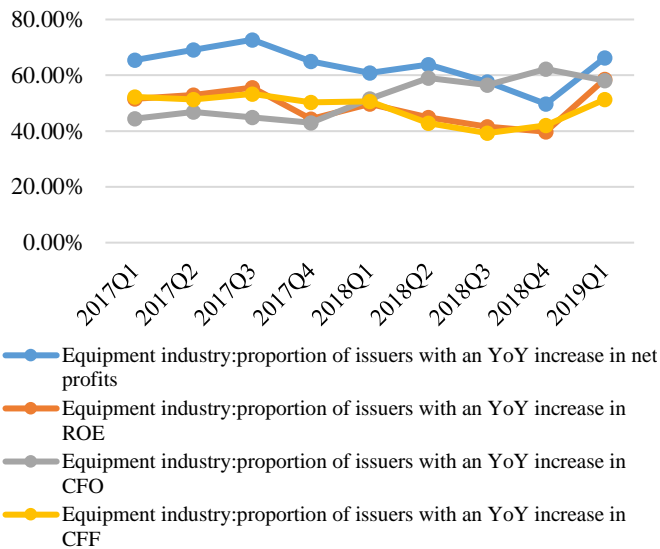
Data source: CCXI

2. Equipment industry: Better cash flow and smaller amount of short-term debts helped to improve short-term solvency

The financial performance of issuers in the equipment industry was mediocre in 2018, and short-term solvency show neither a significant improvement nor a deterioration trend. However, according to the latest financial data for Q1 2019, the profitability, cash flow, short-term debt and short-term solvency of issuers in the industry were all improved. In terms of profitability, two-thirds of the issuers in the industry enjoyed a YoY growth in net profit, and the proportion of issuers with YoY rise in ROE was close to 60%. Both the number of issuers with a growth in CFO and with a growth in CFF exceeded half of the total. Meanwhile, more than 60% of issuers in the industry had less short-term debts YOY, indicating short-term debt pressure was eased significantly. With the improvement of liquidity of most issuers and the alleviation of short-term debt pressure,

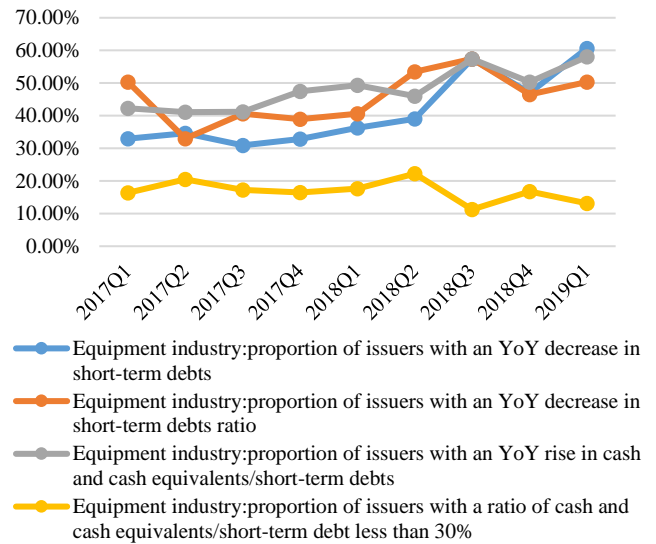
the short-term solvency of equipment industry was significantly improved. The issuers with higher cash coverage ratios accounted for nearly 60%, with a YoY increase of 9 percentage points.

Figure 11: Improvement of CFO and CFF



Data source: CCXI

Figure 12: Short-term debt pressure dropped and nearly 60% of issuers improved solvency

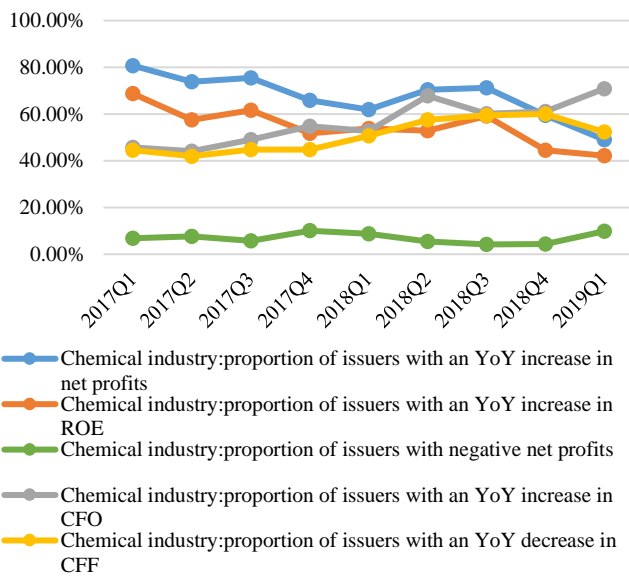


Data source: CCXI

3. Chemical industry: Continuously improved cash flow, better debt maturity structure and enhanced short-term solvency

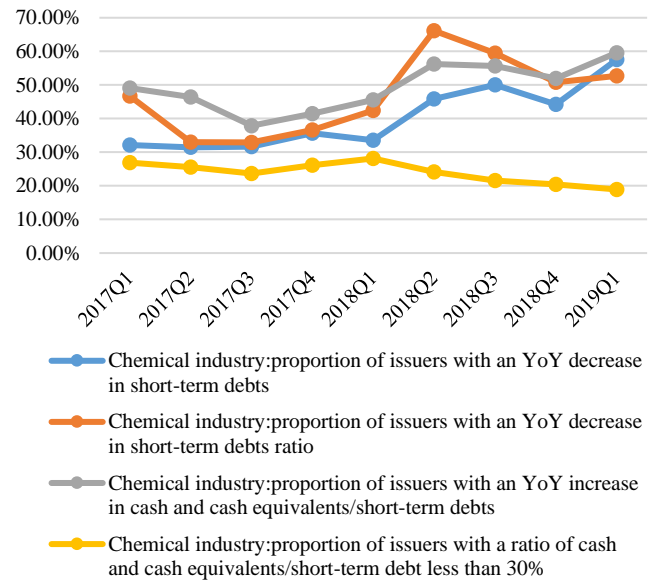
In 2018 and Q1 2019, despite divergent profit performance of the chemical industry, cash flow of most issuers was still improving, and short-term debt ratio continued to decrease, making the short-term debt repayment indicator of most of the issuers in the industry turn better. Specifically, in Q1 2019, issuers with a net profit growth and decline were in equal portions, while the number of issuers suffering a loss increased slightly YoY, and their profit performance continued to diverge. The CFF performance was average, but over 60% of the issuers had an increasing amount of CFO, and the cash flow continued to improve. The debt term structure continued to improve. By the end of Q1 2019, the issuers with less short-term debt and lower short-term debt ratio declined YoY accounted for more than 50%. Overall, the short-term solvency of issuers in the chemical industry continued to improve, and nearly 60% of issuers in the industry showed higher cash coverage ratios.

Figure 13: Continuous improvement of cash flow



Data source: CCXI

Figure 14: Improved debt term structure and higher short-term solvency

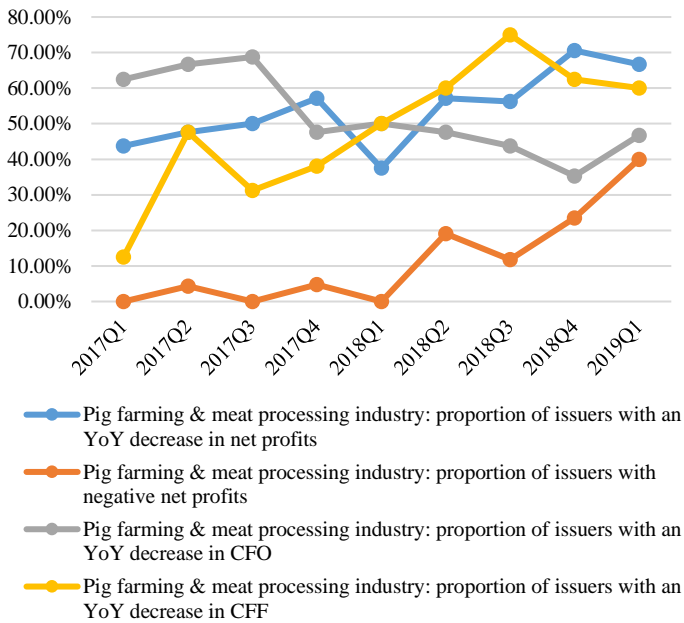


Data source: CCXI

4. Pig farming & meat processing industry: Profit fell sharply, cash flow performance was poor, and short-term solvency of more than 70% issuers was weakened

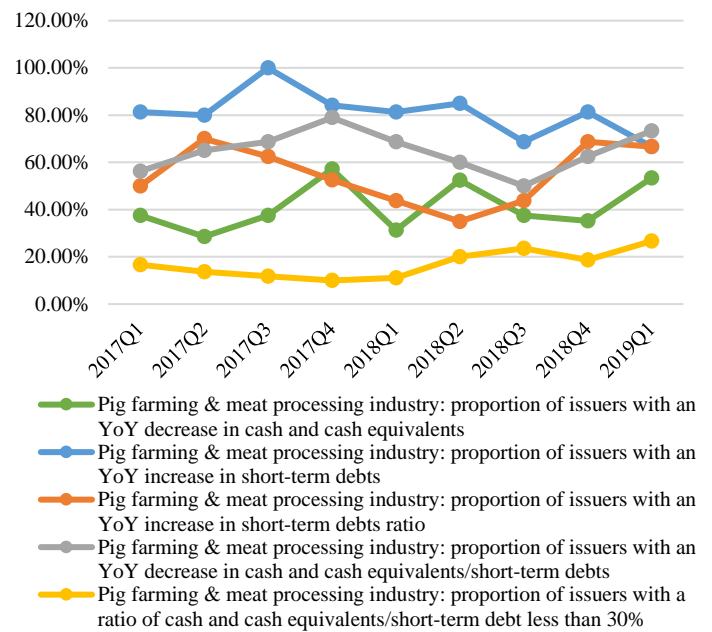
Since 2018, pork prices have been decreased due to hog cycle and hog cholera, and there has been a marked increase in the number of issuers suffering a loss in the pig farming and related meat processing industry. At the same time, due to poor CFF, the cash flow of pig farming industry was poor on the whole, which increased pressure of short-term debts, and the short-term solvency of issuers in the industry was weakened significantly. Specifically, in Q1 2019, two-thirds of the issuers had declined net profit YoY and 40% of issuers suffered a loss in net profit. Nearly 50% and more than 60% of issuers posted decreased CFO and CFF, respectively. The weakened cash flow of most issuers led to a slight decline in cash and cash equivalents. At the end of Q1 2019, more than half of the issuers reported a YoY decline in cash and cash equivalents. At the same time, two-thirds of the issuers showed an expanding trend on the short-term debt, and the short-term solvency of more than 70% of the issuers in the industry was weakened.

Figure 15: Profit declined and cash flow performance was poor



Data source: CCXI

Figure 16: Short-term debt pressure was high and short-term solvency deteriorated

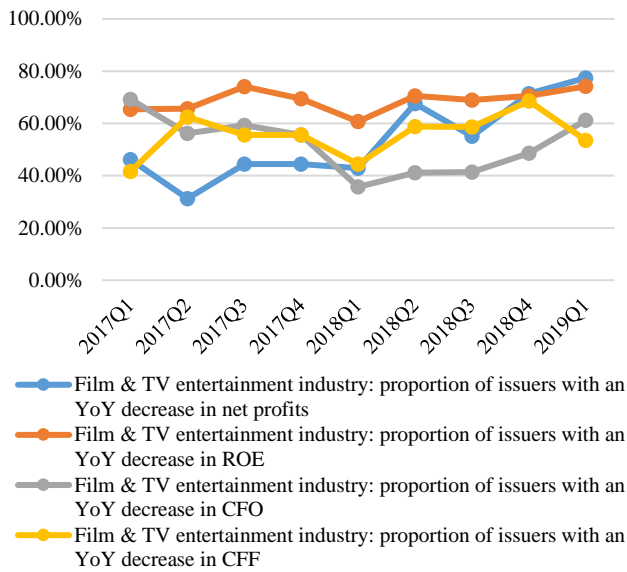


Data source: CCXI

5. Film & TV entertainment industry: Profit and cash flow were poor and short-term solvency declined

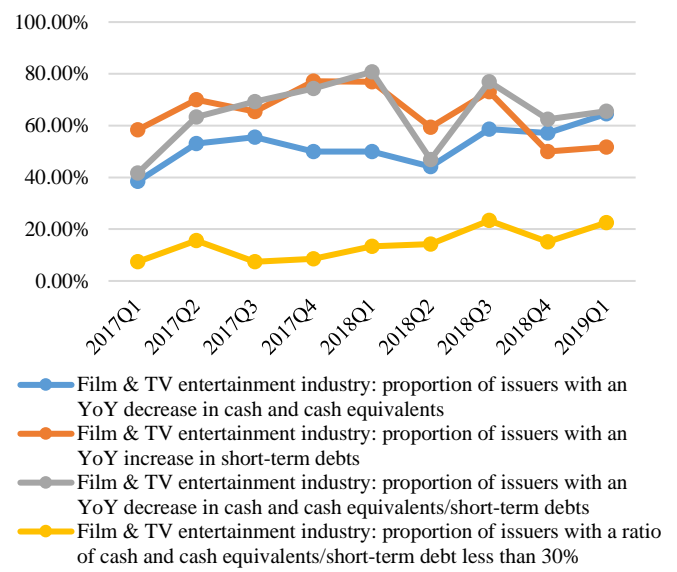
Issuers in the film &TV entertainment industry experienced a significant drop in profitability, CFO, and CFF, resulting in a sharp decline in their short-term solvency. In terms of profitability, in 2018 and Q1 2019, over 70% of the issuers showed a YoY fall in net profit and ROE. As for cash flow, affected by worse operating conditions, more than 60% and 50% of issuers in the industry showed YOY decline in CFO and CFF, respectively, and the proportion of issuers with YoY decline in cash and cash equivalents increased to nearly two-thirds. In terms of short-term debt, although the portion was decreased, more than 60% of the issuers had an increasing amount of short-term debts in the industry than that of last year. Affected by the above performance, the short-term solvency of nearly two-thirds of the issuers in the film & TV entertainment industry were weakened.

Figure 17: Profitability declined, and cash flow performance became weaker



Data source: CCXI

Figure 18: Most issuers showed increased short-term debt and declined short-term solvency

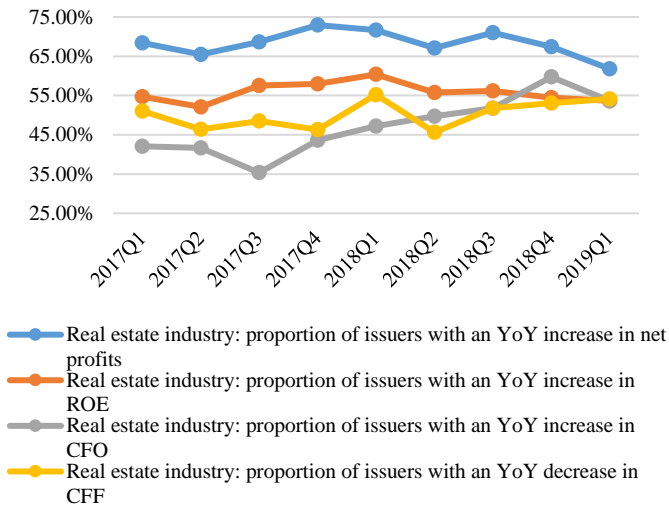


Data source: CCXI

6. Real estate industry: Profits are still rising, but short-term debt continues to increase and the financing environment remains tight

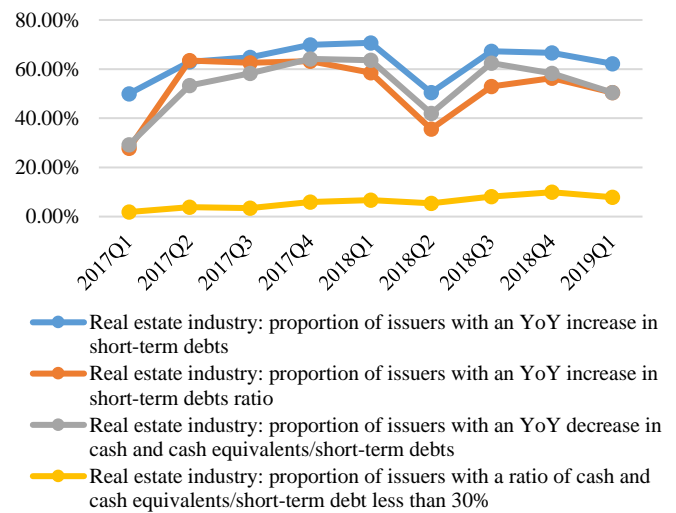
Since 2019, the regulation policies on the real estate industry have been fine-tuned. The real estate market has recovered in the short term, and the profitability of real estate enterprises has been improved, and the fund recovery has been improved remarkably. Under the general principle of “houses are for living, not for speculation”, however, the real estate industry is still under strict regulation and control. The financing environment of real estate enterprises is still relatively tight, and the CFF is poor. The pressure of short-term debt expansion still exists, hindering the short-term solvency of the real estate industry from further improvement. According to financial indicators, in 2018 and Q1 2019, more than 60% of issuers in the industry recorded a YoY increase in net profit, leading to the improvement of the CFO of most of the issuers. However, the performance of CFF has been gradually weakened since the second quarter of 2018, and over 50% of issuers experienced a YOY decrease in net inflows, while more than 60% of issuers in this industry continued to increase short-term debts YOY. Under the increasing pressure of debt rollover, issuers in the real estate industry with better and worse short-term debt servicing indicator were basically in equal portions.

Figure 19: CFF performance remained poor



Data source: CCXI

Figure 20: Short-term debt pressure was high, and short-term solvency has not improved



Data source: CCXI

III. Summary

1. Profit growth slowed down, short-term debt pressure eased, and short-term debt repayment indicator of most issuers were better

Based on the overall financial performance of industrial bond issuers, in 2018 and Q1 2019, total profits of the issuers in the bond market maintained a growth momentum. Their leverage was stable at around 59%, while the proportion of issuers with high leverage (asset-liability ratio $\geq 70\%$) stood at around 27%, which was very close to that of last year. As for short-term debts, the total amount of short-term debts of the issuers continued to decrease YoY, with more than 50% of issuers falling in short-term debts. In respect of cash flow, benefiting from the financing support policies, the shortage of CFF of issuers was slightly mitigated in Q1. Profitability growth enabled CFO to be further improved. Hence, total cash and cash equivalents of issuers maintained a mild growth. Nearly 60% of the issuers showed a YOY increase in cash and cash equivalents, and more than half of them achieved higher cash coverage ratios.

It can be seen that the substantial increase of defaults in the bond market in the first quarter of this year does not mean that the overall credit fundamentals of industrial bond issuers is deteriorating. The latest financial performance reveals that all of the main financial indicators of issuers have been improved to different extents. However, with increasing financing support and moderate fund supply, the credit risk trend of the bond market is actually diverging faster. An increase in defaults is caused by faster liquidation of a small number of issuers with both high credit risk and poor risk resistance in the bond market, while the debt repayment indicators of most of the issuers in the market were improved. On the whole, credit fundamentals of industrial bond issuers have been improved slightly.

2. Solvency decline was recorded in pig farming & meat processing and film & TV entertainment industries, and the financing environment in the real estate industry remained tight. Thus, attention should be paid to subsequent changes in credit risk.

In 2018 and Q1 2019, cash flow of steel & iron and traditional energy, equipment and chemical industries have been improved with different degrees, and short-term debt pressure was eased. Most of the issuers in these

industries have strengthened their short-term solvency. An increasing number of issuers of pig farming & meat processing and film & TV entertainment industries suffered a loss in net profit. Most issuers' CFO and CFF declined, and short-term debt pressure continued to mount, leading to most of the issuers' short-term solvency more weakness. Therefore, attention should be paid to the subsequent credit risk trends of these two industries. Despite further improvement of profitability in the real estate industry, it is necessary to be vigilant about future debt repayment pressure taking into consideration the rising maturity pressure of short-term debts of issuers and tight financing environment.

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