光大水務
EVERBRIGHT WATER

CHINA EVERBRIGHT WATER LIMITED
中國光大水務有限公司

(Incorporated in Bermuda with limited liability)
(Hong Kong Stock Code: 1857)
(Singapore Stock Code: U9E)

RESPONSES TO QUESTIONS RECEIVED FROM SHAREHOLDERS AND THE SECURITIES INVESTORS ASSOCIATION (SINGAPORE)

China Everbright Water Limited (the "**Company**", together with its subsidiaries, the "**Group**") would like to thank all the shareholders of the Company ("**Shareholders**") who submitted their questions in advance of the Company's Annual General Meeting ("**AGM**") which will be convened and held by electronic means on Wednesday, 26 April 2023 at 9:30 a.m. (Singapore time). Due to some overlaps in the questions received, the Company has reorganised and grouped the related and similar questions together, and provided responses accordingly. The Company's responses to the substantial and relevant questions received from Shareholders are set out in Section A.

The Company has also received questions from the Securities Investors Association (Singapore) ("**SIAS**") ahead of the AGM. The Company's responses to the questions received from the SIAS are set out in Section B.

SECTION A: RESPONSES TO QUESTIONS RECEIVED FROM SHAREHOLDERS

1. **It is mentioned on page 16 of the Annual Report 2022 that "as at 31 December 2022, the gearing ratio* of the Group was 61.1%, an increase of 1 percentage point compared to that at the end of 2021". How is the Group's gearing ratio compared to its competitors? Is it higher or lower compared to its competitors? In the current environment of increasing interest rates, is the management of the Company (the "Management") intending to reduce the gearing ratio going forward?**

   The Company's response:

   As at 31 December 2022, the gearing ratio* of the Group was 61.1%, which was lower than the average of gearing ratios of its main competitors which was approximately 64.8%[#] and the gearing ratios of its main competitors[#]. Considering the quality of the Group's existing assets, its profitability and the external market environment faced by it, the most applicable and optimal gearing ratio that the Group should maintain is in the range of 65% to 67%. From the perspective of achieving its long-term strategic goals, there is still room for the Group to increase its gearing ratio. However, taking into account the latest trends of the external economic environment in the next one to three years and the need to balance between business development and risk management, the Group would steadily and gradually achieve its optimal gearing ratio.

   Taking into account its capital expenditure plan for 2023, the Group estimated that, as at 31 December 2023, its gearing ratio would not be higher than 63% and its debt-to-equity ratio would be maintained at not more than 169%.

   The Group has been monitoring and controlling its gearing ratio and finance costs. In particular, the Group had been exploring various financing methods in and outside mainland China to diversify its financing channels. The Group is of the view that the diverse financing channels complement each other as they enhance the flexibility of its financing to achieve a balance between equity financing and debt financing and optimise its financing structure. As a result, the Group is able to actively develop its businesses while solidifying its financial position, providing a solid foundation for its long-term development. Through the multiple financing channels, the Group could plan and control the proportion of its long- and short-term loans, the proportion of its loans denominated in RMB and foreign currencies, the proportion of its loans at floating and fixed rates, the replacement of short-term loans with long-term ones, and the replacement of the high-interest rate loans with low-interest rate loans in a flexible and reasonable manner. This enables the Group to better control its finance costs and manage the potential exchange rate risks and liquidity risks.

This was especially true in 2022 as the monetary policies of China and America diversified due to their different economic situations.

On the one hand, mainland China maintained a moderately loose monetary policy: the 5-year loan prime rate ("**LPR**") was adjusted 3 times during the year, reducing from 4.65% in December 2021 to 4.30% in December 2022. In April 2022, the People's Bank of China reduced the required reserve ratio by 0.25 percentage points. Capital market interest rates also remained low. For example, the 3-year pricing of China Development Bank RMB Bond Yield remained stable at around 2.50%.

On the other hand, under the pressure of inflation, the Federal Open Market Committee of the Federal Reserve had increased its federal fund rate by a total of 425 basis points during 2022, resulting in a significant increase in London Interbank Offered Rate ("**LIBOR**") or Secured Overnight Financing Rate ("**SOFR**"), which are the benchmark interest rates for loans denominated in United States dollars ("**USD**"), and the Hong Kong Interbank Offered Rate ("**HIBOR**"), which is the benchmark interest rate for loans denominated in Hong Kong dollars ("**HK$**"), during 2022.

The Group has closely monitored the interest rate trends in and outside mainland China. Through the issuance of RMB-denominated bonds (such as the issuance of the second tranche of super & short-term commercial papers ("**SCPs**") with a principal amount of RMB1 billion and an interest rate of 2.50% in January 2022, the issuance of the third tranche of medium term notes ("**MTNs**") with a principal amount of RMB1 billion and an interest rate of 3.10% in April 2022, the issuance of the first tranche of perpetual MTNs with a principal amount of RMB700 million and an interest rate of 3.30% in June 2022 and the issuance of the third tranche of SCPs with a principal amount of RMB1 billion and an interest rate of 1.72% in September 2022), repricing of project loans, preferential interest rate policies and other methods, the Group has adjusted the proportion of its loans denominated in RMB and foreign currencies (the proportion of loans denominated in foreign currencies decreased from 32% at the end of 2021 to 26% at the end of 2022) and the interest rate structure, therefore offsetting some of the negative impacts arising from the increase of interest rates outside mainland China. The Group expects that the high interest rate environment outside mainland China will continue for some time, and therefore shall pay close attention to the changes in the market and continue to reduce the proportion of its loans denominated in foreign currency, thereby reducing its finance costs.

In addition to adjusting the loan structure, the Group also actively expanded its asset-light business such as operation and management ("**O&M**"), so as to reduce loans while increasing income, thereby slowing down the speed and scale of the increase in gearing ratio. In 2022, the number of O&M projects undertaken by the Group increased from three at the end of 2021 to five at the end of 2022. With its extensive O&M experiences and continuous innovation of technology, the O&M business will be the focus of the Group's development.

* the gearing ratio = total liabilities over total assets

\# The gearing ratios of the Group's main competitors (which are the top three industry players in China) are calculated by the Group based on the annual results of its main competitors for the financial year ended 31 December 2022 ("**FY2022**").

2. **On page 11 of the FY2022 Annual Results Presentation, the trade receivables recovery rate for the full year period had dropped to 72% in FY2022, a decrease of 12% compared to the financial year ended 31 December 2021 ("FY2021"). Is the Management able to explain what are the factors that have caused the drop in recovery rate? How much of these "yet to recover" trade receivables are going to end up as non-recoverable and "write-off"? What is the Management doing to improve the recovery rate to more than 90%?**

The Company's response:

The Company's trade receivables recovery rate for FY2022 was 72%, representing a decrease from the trade receivables recovery rate of 84% for FY2021. The decrease was mainly due to the impact of the COVID-19 pandemic on the settlement of waste water treatment service fees by local governments, resulting in a slowdown in payment progress. Since the outbreak of the COVID-19 pandemic in China in early 2020, the economic activities in various regions of China have been significantly reduced or delayed due to the lockdown imposed in various regions to control the recurring pandemic. Furthermore, the local governments had introduced a number of tax and social security relief policies for the benefit of the citizens and enterprises, resulting in a drastic reduction in the local governments' revenue, which were mainly composed of tax revenue. In addition, the various measures implemented by local governments to prevent and control the pandemic substantially increased their expenditures. Therefore, the local governments recorded declining revenues and increasing expenditures during the period. Moreover, the finances of the local governments were even tighter in 2022, which was the third year after the outbreak of the COVID-19 pandemic. With pandemic control being the priority of local governments, the payments of other expenses including waste water treatment service fees slowed down.

The customers of the Company's trade receivables are mainly local governments. As such, despite the delay in payment of the trade receivables, the risk of default is quite low. Therefore, it is expected that the trade receivables will be gradually recovered in the future and will not be written off.

Managing trade receivables is at all times the key focus of the Management. The Management monitors the recovery of trade receivables on a monthly basis and regularly reviews the ageing analysis of trade receivables and other reports to continuously monitor credit risk. For trade receivables in large amounts or with long ageing, the Company ensures that the responsibilities are delegated to specific persons in charge, and the Management also personally supervises and pays close attention to the recovery of trade receivables.

The Group believes that, following the relaxation of the COVID-19 control measures and lifting of travel restriction by the Chinese government at the end of 2022, the economic activities in various regions have resumed. The focus of local governments will shift from pandemic control to economic development, and the payment of waste water treatment services fees will be accelerated accordingly.

3. **The biggest concern is the huge negative net cash flow from operating activities amounts to HK$640 million which is due mainly to the increase in trade receivables of HK$1.31 billion. Why are the situation of trade receivables so bad considering that most of the customers are local governments?**

The Company's response:

Regarding the recovery of trade receivables from local governments, please refer to the Company's response to question 2 above.

With regard to cash flows from operating activities, the Group recorded net cash outflows from operating activities mainly due to the increase in contract assets. The increase in contract assets represents the cash flows in relation to the construction expenditure (i.e. capital expenditure) arising from the Group's investment and construction of concession projects with guaranteed revenue (i.e. projects with guaranteed minimum water volume). This portion of cash flows is classified as cash flows from operating activities, rather than as cash flows from investing activities according to IFRIC 12 under the International Financial Reporting Standards. Therefore, following the increase in the Group's business scale as well as the increase in the investment and construction of the concession projects, it will likewise increase in the negative cash flow from operating activities.

According to the calculation done by the Group, if the cash flows from capital expenditures associated with the construction of concession projects were reclassified as cash flows from investing activities, the Group's net cash flows from operating activities for each year would have been positive. In 2022, even with the increase of trade receivables amounting to HK1.31 billion, the net adjusted cash flow from operating activities would have been approximately HK$1.074 billion (2021: HK$1.460 billion).

4. There was a trade receivables impairment allowance of HK$447 million. Again, considering that most of the customers are local governments, why is the impairment so high?

The Company's response:

As mentioned in the Company's response to question 2 above, 2022 is the third year after the outbreak of the COVID-19 pandemic in China since early 2020, and the local government's finances have become increasingly tight during the pandemic. With the pandemic control being the priority of local governments, the payments of other expenses including waste water treatment service fees slowed down accordingly. As a result, the trade receivables recovery rate decreased from 92% for FY2020 to 72% for FY2022. The ageing of trade receivables has become longer, the amount of overdue trade receivables also increased. Although there was no default by any local government from year 2020 to year 2022, the delay in the recovery of trade receivables, the drop of the trade receivables recovery rate, the deterioration in the ageing of trade receivables and the increase in the amount of overdue trade receivables are all objective signals of significant increase in credit risk.

In response to the above, the Management has adopted a more prudent approach in assessing the provision for impairment of trade receivables – provision for impairment was not only made for trade receivables with longer ageing in the current period, but also for the risk assessment for each project throughout the operation period in accordance with principle as set out in IFRS 9 (Expected Credit Losses), rather than only for losses incurred. Although most of the customers are local governments, the Group is required to recognise provision for impairment of trade receivables under objective circumstances where there is a significant increase in credit risk.

5. **There has been a drop in revenue for FY2022. Was it a deliberate choice by the Group to focus less on construction projects for the year? Or was there another reason that truly accounted for the fall in revenue?**

The Company's response:

Construction service revenue decreased by HK$694.71 million or 22% from HK$3.09845 billion in FY2021 to HK$2.40374 billion in FY2022. Construction activities in FY2022 were affected by the recurring COVID-19 pandemic in China, resulting in delays in construction progress and a decrease in construction activities. Construction service revenue remains a significant component of the Group's revenue. However, following the increase in the number of projects which have completed and have commenced operation, both the absolute value and proportion of operation income increased significantly, generating more cash flows for the Group.

6. **Can the board of directors (the "Board") of the Company consider carving out assets into a real estate investment trust fund ("REITs") for water services and return the proceeds to the Shareholders? This will close the big gap between trading price and net asset value.**

The Company's response:

Following the joint issuance of the "Notice of the Work Related to Promoting the Pilot Program of Real Estate Investment Trusts (REITs) in the Infrastructure Field" by the China Securities Regulatory Commission and the National Development and Reform Commission since 30 April 2020, the Company has closely followed the policies of REITs and market issuance dynamics. In addition, it communicated with external regulators and external service providers, studied the precedents, and, in combination with the Company's own situation, conducted extensive research on various aspects of REITs, such as selection of projects, transaction structures, tax impacts, impacts on financial statements, etc.

In general, REITs can liquidate the existing assets of the Company, broaden the sources of project construction funds, and form a virtuous circle of investment and financing. At the same time, REITs can also reduce the gearing ratio and narrow the gap between the trading price and the net asset value effectively.

Currently, the Company has carried out preliminary works and due diligences, and maintained regular and comprehensive communications with the external service providers.

The Company will continue monitoring the relevant policies and market developments, steadily carry out various tasks of REITs and based on the prevailing market conditions and its own situation, decide whether to proceed with REITs or not, and will provide the latest information to the Shareholders as and when appropriate.

SECTION B: RESPONSES TO QUESTIONS RECEIVED FROM SIAS

1. **For FY2022, the Group reported a decrease in revenue of 3% to HK$6.73 billion. The Group's gross profit decreased by 8% and profit attributable to equity holders of the Company decreased by 16% compared to FY2021. Accordingly, earnings per share have declined from HK$0.4196 to HK$0.3532.**

   (i) **Revenue: In Note 5 (page 219 of the 2022 Annual Report – Revenue), the breakdown of revenue shows that construction service revenue from service concession arrangements fell sharply from HK$3.1 billion to HK$2.4 billion. Construction service revenue is measured based on the Group's estimation of the fair value of construction services and the percentage of construction completed during FY2022. What are the reasons for the decrease in construction service revenue from service concession arrangements?**

5. REVENUE　　5. 收入

		Year ended 31 December 截至十二月三十一日止年度	
		2022 二零二二年 HK$'000 千港元	2021 二零二一年 HK$'000 千港元
Construction service revenue from service concession arrangements	服務特許經營權安排的建造服務收入	2,403,740	3,098,448
Finance income from service concession arrangements	服務特許經營權安排的財務收入	1,107,945	1,068,040
Operation income from service concession arrangements	服務特許經營權安排的運營收入	2,950,629	2,522,688
Construction contract revenue and technical service income	建造合約收入及技術服務收入	265,653	223,195
		6,727,967	6,912,371

(Source: 2022 Annual Report; emphasis added)

The Company's response:

Construction service revenue decreased by HK$694.71 million or 22% to HK$2.40374 billion in FY2022 from HK$3.09845 billion in FY2021. The construction activities during FY2022 had been affected by the recurring COVID-19 situation in China, which led to delay in construction progress and a drop in construction activities.

(ii) If the decrease was due to COVID-related disruptions, have the Group's operations been fully restored upon the lifting of all or most of the COVID-related measures in China since January 2023?

The Company's response:

Since December 2022, the Chinese government has relaxed the COVID-19 control measures and lifted various local travel restrictions. Furthermore, the Chinese government has launched a series of new expansionary fiscal policies, as it strived to quickly recover and develop China's economy. As a result, since January 2023, various aspects of the Group's business have gradually recovered from the negative impacts caused by the pandemic. While the current macro-economic environment and market conditions are still recovering and remain uncertain, the Group will take proactive actions and make comprehensive plans to carry out various aspects of its business in an orderly manner.

(iii) 14th Five-Year Plan: For the benefit of Shareholders, could the Management highlight the major opportunities created by the 14th Five-Year Plan? What is the "adjustment period" mentioned in the CEO's report (page 7 of the 2022 Annual Report)?

The Company's response:

In 2021, China issued the outline of the 14th Five-Year Plan (2021-2025) for National Economic and Social Development and the Long-Range Objectives Through the Year 2035 (《中華人民共和國國民經濟和社會發展第十四個五年規劃和2035年遠景目標綱要》) and "14th Five-Year Plan" for Urban Waste Water Treatment and Resources Utilisation Development (《「十四五」城鎮污水處理及資源化利用發展規劃》). In these plans, the main opportunities are:

a) the centralised collection rate of urban domestic waste water will reach over 70% by 2025, and it is expected that 80,000 km of wastewater collection pipeline network will be newly constructed and upgraded;

b) the waste water treatment capacity in cities and counties shall basically meet the needs of economic and social development and the waste water treatment rate in counties shall reach over 95%, and it is expected to increase the waste water treatment capacity by 20 million m^3/day;

c) the utilisation rate of reusable water in water-deficient cities at and above the national prefecture level will reach over 25% and the Beijing-Tianjin-Hebei region will reach over 35%, while water-deficient cities at and above the prefecture level along middle and lower reaches of the Yellow River Basin will reach 30%, and it is expected that the total production capacity of reusable water of newly-built, upgraded and expanded facilities will be no less than 15 million m^3/day; and

d) the urban harmless sludge treatment capacity will reach over 90%, and it is expected that the total capacity of new harmless sludge treatment facilities will be no less than 20,000 tonnes/day (water content: 80%).

However, after nearly 20 years of rapid development, the traditional water industry had gone through its rapid development stage and is now becoming saturated. The industry will gradually move from "rapid growth" to "precision and high-quality development". The "adjustment period" means that during the "14th Five-Year Plan" period, the water industry will focus on "overcoming shortcomings", "improving weaknesses", "recycling" and "harmlessness" and put the emphasis on "high-quality development" instead of rapid growth.

While focusing on improving and enhancing the quality of its traditional business, the Group is also proactively monitoring the industry trends and searching for a breakthrough in new business areas such as industrial waste water, sludge disposal, solar photovoltaic and other business areas. Recently, the Group successfully secured Jiangyin High-tech Zone Industrial Waste Water Treatment Plant Phase I (EPC+O) Project with the treatment capacity of 30,000 tonnes/day, Liaoning Anshan Municipal Sludge Disposal Project Phase I with a capacity of 500 tonnes/day, and installed six sets of solar power generation supporting facilities at its projects, with the total capacity of such facilities installed in the pilot project plant areas exceeding 8 MW.

In addition, the Group will focus on the "water-related business" and explore new business areas and directions, such as "rural revitalisation", "ecological agriculture" and "green and low-carbon" in depth by deeply studying the industry policies with its key development areas.

(iv) **Trade receivables: As at 31 December 2022, the Group had trade receivables amounting to HK$3.36 billion, net of expected credit losses (ECL) allowance of HK$446.8 million. The recoverability of trade receivables is also a key audit matter highlighted by the auditors in their report. Total carrying amount of trade receivables are nearly 50% higher at HK$3.81 billion as at 31 December 2022 while impairment has increased by over 77% from HK$252.0 million to HK$446.8 million (page 259 of the 2022 Annual Report). In particular, trade receivables past due by over 13 months amount to HK$851.8 million (page 258 of the 2022 Annual Report), nearly three times the level in FY2021. Can the Management help the Shareholders better understand the severity of the challenges faced by the local governments? What efforts have the Management made to collect on the long-outstanding debt? What recourse, if any, does the Group have?**

The Company's response:

The increase in the Group's total trade receivables was mainly due to the local governments' settlement for waste water treatment service fees being affected by the COVID-19 pandemic, which resulted in a slowdown in payments. Since the outbreak of the COVID-19 pandemic in China at the beginning of 2020, the economic activities in various parts of China were substantially reduced or delayed due to the lockdown imposed in various regions to control the recurring pandemic situation. Furthermore, the local government had introduced several tax and social security relief policies for the benefit of citizens and enterprises, resulting in a drastic reduction in the local government's revenue of which tax revenue forms a main part. Besides, during the COVID-19 pandemic, the various measures implemented by local governments to prevent and control the pandemic substantially increased expenditures. Therefore, the local governments recorded declining revenues and increasing expenditures during the period. Furthermore, the finances of the local governments were even tighter in 2022, which was the third year of the outbreak of the COVID-19 pandemic. With the pandemic control being the priority of local governments, the payments of other expenses including waste water treatment service fee slowed down accordingly.

Managing trade receivables is at all times the key focus of the Management. The Management monitors the recovery of trade receivables on a monthly basis and regularly reviews the ageing analysis of trade receivables and other reports to continuously monitor credit risks. For trade receivables with large amounts and long ageing, the Company ensures that the responsibilities are delegated to specific persons in change, and the Management also personally supervises and continuously pays attention to the recovery of trade receivables.

2. **As at 31 December 2022, the Group had outstanding borrowings of HK$15.26 billion, representing an increase of HK$820.20 million as compared to HK$14.44 billion as at the end of 2021. The borrowings included secured interest-bearing borrowings of HK$2.29 billion and unsecured interest-bearing borrowings of HK$12.97 billion. The Group's borrowings are mainly denominated in RMB, accounting for approximately 74% of total borrowings, while the remainder is denominated in HK$, USD and euros ("EUR"). Most of the Group's borrowings are at floating rates.**

   (i) **What is the Management's view on the interest rates trends in the People's Republic of China (the "PRC" or "China").**

   The Company's response:

   In 2022, China's economy experienced downward pressure with an uncertain financial market due to various unexpected factors such as the frequent and dispersed pandemic outbreaks, the downturn of real estate cycle, the Russo-Ukrainian crisis and the persistent interest rate hikes outside mainland China. In order to balance between pandemic prevention and control and social-economic development, the overall market liquidity remained loose, with major interest rates in mainland China showing a downward trend and the financing costs of the real economy maintaining at a low level.

   In 2023, the foundation for economic recovery is still not solid. In view of the need to stabilise growth and expand domestic demand, it will be difficult to tighten the monetary policy in 2023, which focuses on both total quantity and structure, with the financing costs of the real economy maintaining at a lower range.

   In the recent first quarter, the People's Bank of China decided to cut the required reserve ratio of financial institutions by 0.25 percentage point on 27 March 2023. Therefore, the overall market liquidity will remain loose in the coming year, with interest rates maintaining at the current level.

The Management has stated that the Group does not use financial derivatives to hedge against interest rate risk. Based on the sensitivity analysis, a general increase/decrease of 1% in the interest rates, with all other variables held constant, would decrease/increase the Group's profit before tax by approximately HK$123.1 million.

(ii) Can the Board, especially the Audit Committee, help Shareholders better understand the deliberations it has had on hedging the group's interest rate risks? How costly would it be to hedge the Group's interest rate risks?

The Company's response:

Notwithstanding that the Group's principal businesses are located in mainland China, the Group borrows loans denominated in both RMB and non-RMB currencies to diversify its source of financing. The Group's structure of borrowings is relatively simple, which is mainly affected by the fluctuation of a few benchmark interest rates, such as LIBOR/SOFR, HIBOR and 5Y-LPR. In addition, the aforementioned benchmark interest rates were relatively stable in the past. Therefore, the Group's response to interest rate risk is mainly to monitor interest rates trends by adjusting the structure of borrowings through adjusting the proportion of long- and short-term loans, the proportion of loans denominated in RMB and non-RMB currencies as well as the proportion of loans at floating and fixed interest rates.

In 2022, by referring to the interest rate trends in and outside mainland China, the Group made various adjustments to the interest rates and the proportion of currencies of its financings in order to minimise some of the negative impacts arising from the increase in interest rates outside mainland China, such adjustments including:

a) re-determining the interest rates of all project loans and credits in mainland China with a single fluctuation range of 85-135 basis points;

b) seizing the opportunity to issue RMB-denominated bonds at fixed rates during the good window period, such as the issuance of the second tranche of SCPs with a principal amount of RMB1 billion and an interest rate of 2.50% in January 2022, the issuance of the third tranche of MTNs with a principal amount of RMB1 billion and an interest rate of 3.10% in April 2022, the issuance of the first tranche of perpetual MTNs with a principal amount of RMB700 million and an interest rate of 3.30% in June 2022, and the issuance of the third tranche of SCPs with a principal amount of RMB1 billion and an interest rate of 1.72% in September 2022, in order to replace some floating-rate loans; and

c) adjusting the proportion of its loans denominated in RMB and foreign currencies to leverage on the downward trend of interest rates for the loans denominated in RMB and the upward trend of interest rates for loans denominated in foreign currencies such as USD and HK$. As such, the proportion of loans denominated in foreign currencies decreased by 6 percentage points from 32% at the end of 2021 to 26% at the end of 2022.

The costs to hedge interest rates depend on the types of the financial derivatives to be used and according to the negotiations and arrangements with the banks or financial institutions.

(iii) How frequently are the borrowings repriced?

The Company's response:

The Group's borrowings include project loans from banks in mainland China, liquidity loans from banks in mainland China, liquidity loans from banks outside mainland China and bonds issued in the open markets, the details of which are as follows:

a) the repricing cycle for the interest rates of project loans and domestic liquidity loans obtained from the banks in mainland China normally is 12 months;

b) the repricing cycle for liquidity loans obtained from the banks outside mainland China normally includes 1 month, 3 months and 6 months; and

c) the interest rate of bonds issued in the open markets of mainland China is fixed and remained the same within the period.

The Group has cooperated with various credit banks for a long time and maintained a good relationship. Although the Group has signed credit contracts with the banks for each credit limit, the Group can approach and discuss with the banks about the re-pricing plan in a timely manner according to the market conditions, in order to ensure that the credit conditions are in line with the market and in the Company's interests.

(iv) SCPs: During FY2022, the Company issued super SCPs, MTNs and perpetual MTNs. What are the benefits of issuing SCPs? Could the extensive use of SCPs create a duration mismatch? How deep is the SCPs market and is there a risk that the SCPs market may not be available when the Company needs to rollover its SCPs as they mature?

The Company's response:

SCPs have the characteristics of low interest rate, large issuance amount and simple issuance procedures.

In 2022, the issuance scale of traditional credit bonds in China, comprising the SCPs in the national inter-bank bond market of mainland China, MTNs in the national inter-bank bond market of mainland China and corporate bonds at the Shanghai Stock Exchange, was RMB12.1 trillion, of which the issuance scale of SCPs was RMB4.43 trillion, accounting for 37% of the total issuance scale. It is one of the most important types of credit bonds and the market was very mature.

The issuance of SCPs facilitates the reduction of finance cost of the Company. At any point of time, the outstanding SCPs of the Group shall not exceed RMB1 billion, which was relatively small in amount as compared with the total issuance scale and therefore less risky.

The registered principal amount of SCPs has a revolving nature within the validity period as set out in the notice of registration acceptance, provided that the outstanding amount of SCPs at any point of time shall not exceed the registered principal amount. Upon the maturity of the SCPs, a new tranche of SCPs will be issued for repayment purpose and the investors are usually banks.

The Group will make a filing with National Association of Financial Market Institutional Investors of the PRC one to two weeks before the issuance, and the issuance can be made after the filing is successful. Therefore, the problem of unsuccessful issuance does not exist. In addition, as at 31 December 2022, the Group had cash on hand and bank balance in and outside mainland China of approximately HK$2.846 billion, with the unutilised banking facilities amounting to approximately HK$3.893 billion. In March 2023, the Group also obtained the notice of registration acceptance for the issuance of MTNs with a registered principal amount of RMB5 billion (i.e. the issuance limit). All of these can be withdrawn/issued at any time to redeem the SCPs upon their maturity.

3. **In the Group's risk assessment, two risks have been identified as particularly heightened:**

- **New business investment and market competition risks (page 24 of the 2022 Annual Report); and**

- **Accounts receivable risk (page 25 of the 2022 Annual Report).**

No. 序號	Name of risk 風險名稱	Effectiveness of control measures 管控措施是否有效	Changes of trend in risk level *(Note)* 風險等級變化趨勢 *(附註)*
1	Policy changing risk 政策變動風險	Effective 有效	→
2	New business investment and market competition risks 新業務投資與市場競爭風險	Effective 有效	↑
3	Environmental compliance and safe production management risks 環境合規與安全生產管理風險	Effective 有效	→
4	Accounts receivable risk 應收賬款風險	Effective 有效	↑

(Source: 2022 Annual Report; emphasis added)

(i) New business investment and market competition: Can the Management help Shareholders better understand the market dynamics of the environmental water industry in the PRC? Has there been any consolidation and what is the Group's market share in the PRC? What is the Group's competitive advantage? In addition, how much research and development ("R&D") does the Group carry out and how strong is the Group's R&D function?

The Company's response:

According to the "14th Five-Year" Plan, the development of the water industry is shifting from "rapid development" to "high-quality" development with more stringent requirements being imposed on the industry. Therefore, the water enterprises will face severe challenges. As its next course of action, the Group will strictly follow the industry requirements and industry trends arising from the "pollution and carbon reduction, green and low-carbon" initiatives, seizing the market opportunities of "resource utilisation" and strengthening the precision management of existing projects. By deeply tapping into the potential, opening up sources, reducing costs and increasing efficiency, the Group can achieve effective qualitative improvement. The Group will continue to solidify its market position in advantageous areas and develop high-quality projects actively, so as to achieve reasonable quantitative growth.

There are quite a number of environmental protection companies in China. Hence, the market share concentration is relatively low. In recent years, due to various factors such as policy changes and overall capability, the market share of private enterprises showed a downward trend. Currently, the market share is primarily dominated by central government-owned enterprises and state-owned enterprises. As of 31 December 2022, the total water treatment capacity of the Group was approximately 7.25 million m^3/day and ranked among the best in China in terms of its treatment capacity and operation quality. The Group was selected as one of the "Top Ten Influential Enterprises in China's Water Industry" for the fifth consecutive year.

The competitive advantages of the Group are as follows: (i) as a leading water environment solution provider in China, the Group has benefited from the favourable policies promulgated by the Chinese government and the rapid development of the water industry; (ii) the Group has extensive experiences in providing various types of water environment solutions and has sufficient ability to seize market opportunities and explore new service combinations; (iii) the Group has a reliable track record and healthy project pipeline to support the endogenous growth of the Group and great potential for acquisition and expansion; (iv) the Group is committed to developing core technologies and having strong R&D capabilities; (v) leveraging on the "Everbright" brand, the Group has unparalleled competitive advantages and growth prospects; and (vi) the Group has an experienced, market-oriented and strong executive management team.

By focusing on its strategic direction and the industry development trend, the Group places great importance on R&D activities and has a professional R&D team. The Group has a technology research centre in China with experts from various fields of technology. The Group has also incorporated a joint venture company (E+B Umwelttechnik GmbH) in Germany, the principal business of which includes the R&D in the water sector, bringing in and introducing advanced global environmental protection technologies. The Group's R&D activities mainly focus on areas such as the synergy between pollution and carbon reduction, monitoring and calculation of carbon emissions, ozone-oxygen separation as well as freeze-drying crystallisation and concentration. Furthermore, it has developed a number of technological processes including shortcut nitrification and denitrification, biochemical treatment E-BioFAS, FBR-Fenton, freeze-drying crystallisation and concentration, intelligent water resources protection and ozone-oxygen separation. These technologies are not only applied to new projects, but also provide effective support for existing projects. For example, the Group has applied its ozone-oxygen separation technology in the ozone catalytic oxidation process section of Lingxian Wastewater Treatment Plant in Dezhou with high separation degree, stable operations and obvious effects. The oxygen recovery rate is over 95% and 70% of the liquid oxygen is saved.

(ii) Accounts receivable: It was reported by S&P Global that many local governments in the PRC have breached the unofficial thresholds* with their direct debt exceeding 120% of their revenues in 2022. How much consideration is given to the creditworthiness of the local PRC governments before signing any major projects? What safeguards are put in place to ensure that the group's interests are well protected, regardless of the state of the local economy?

* *extracted from https://www.spglobal.com/ratings/en/research/articles/230221-the-clock-is-ticking-for-the-debt-led-growth-of-china-local-governments-12642869*

The Company's response:

The Group has been very prudent in considering the economic and financial capabilities of local governments. Generally speaking, the Group prefers to secure projects in the following regions:

a) Beijing-Tianjin-Hebei region, Yellow Bohai Sea, Yangtze River Delta, southeast coastal areas and cities in Guangdong-Hong Kong-Macau Greater Bay Area; and

b) provincial capital cities, prefecture-level cities and top 100 counties in other regions with better fiscal revenue.

The Group and the general managers of its project companies have established and maintained a healthy and efficient communication mechanism with local governments, as an effort to ensure timely payments in accordance with the agreements. The Group and the project companies actively urge local governments to include water treatment service fees into their annual budgets to ensure the source of payments. In addition, the Group will also leverage on the influence, geographical and network advantages of China Everbright Group Ltd. (the controlling shareholder of China Everbright Environment Group Limited, which in turn is the controlling shareholder of the Company), and coordinate with the local governments to ensure timely payment of water treatment service fees.

IMPORTANT NOTICE

This announcement is for information purposes only and does not constitute or form a part of any offer, solicitation or invitation to sell, issue, purchase or subscribe for securities in any jurisdiction. No securities of or relating to the Company have been or will be registered under the securities laws of any jurisdiction. No public offering of securities will be made in any jurisdiction where such an offering is restricted or prohibited. No money, securities or other consideration is being solicited by this announcement or the information contained herein and, if sent in response to this announcement or the information contained herein, will not be accepted.

By Order of the Board
China Everbright Water Limited
Kwan Yun Fui
Legal Counsel and Joint Company Secretary

Hong Kong and Singapore, 25 April 2023

As at the date of this announcement, the Board comprises: (i) three executive directors, namely Mr. Hu Yanguo (Chairman), Mr. Tao Junjie (Chief Executive Officer) and Mr. Luo Junling; and (ii) four independent non-executive directors, namely Mr. Zhai Haitao, Mr. Lim Yu Neng Paul, Ms. Cheng Fong Yee and Ms. Hao Gang.