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CCXAP affirms Sino-Ocean Group Holding Limited's long-term credit rating at BBB$_g$+, with stable outlook

Hong Kong, 12 October 2020 -- China Chengxin (Asia Pacific) Credit Ratings Company Limited ("CCXAP") affirms the BBB$_g$+ long-term credit rating of Sino-Ocean Group Holding Limited ("Sino-Ocean" or the "Company"), with stable outlook. Sino-Ocean's rating reflects that the Company's sufficient and high-quality land bank and strong shareholder support from China Life Insurance (Group) Company Limited ("China Life"). However, the rating is also constrained by depressed contracted sales due to outbreak of COVID-19 and less saleable resources in 2020H1.

Corporate Profile

Sino-Ocean was established in 1993 and listed on the Hong Kong Stock Exchange (Stock Code: 3377.HK) in 2007. Sino-Ocean is one of the leading property developers in Mainland China with a land bank distribution across 6 core regions of China, as well as Indonesia and Singapore. The Company had a presence in 51 cities and owned nearly 200 projects at mid-2020. As of 30 June 2020, China Life Insurance (Group) Company Limited ("China Life") and Dajia Insurance Group Co., Ltd. ("Dajia Insurance", formerly known as Anbang Insurance Group Co., Ltd.) were the two major shareholders that held 29.59% and 29.58% of the Company's shares, respectively.

Rating Rationale

Credit Strengths

Sufficient and high-quality land banks. As at 30 June 2020, Sino-Ocean has a total land bank 37.4 million sqm, which would be sufficient for its development for the next 4-5 years. About half of the total land bank located in Beijing Region (28%) and Bohai Rim Region (26%). For the rest of the land bank, Southern Region accounted for 16% of the land bank, followed by Eastern Region (10%), Central Region (10%) and Western Region (10%). A relatively concentrated distribution in Beijing and its surroundings may imply that the Company had a high exposure to the regulation risks in these regions. Nonetheless, the Company's land bank in the city clusters with strong economic prospects and continuous population inflow is expected to support its contracted sales over the next 12-18 months.

Sino-Ocean accelerated land replenishments in 2020H1, acquiring 18 projects with gross floor area of 2.0 million sqm at an attributable cost of RMB8.5 billion, significantly increased as compared to that of 1.0 million sqm and RMB2.6 billion in 2019H1. In 2020, Sino-Ocean proposed the new "south and west" strategy, which aimed at switching investment focus from Beijing and surrounding regions to Yangtze Delta Region, Greater Bay Area, Western Region and Central Region to diversify land bank distribution. About 72% of the newly acquired land projects by gross floor area in 2020H1 were located in Eastern Region, Southern Region, Western Region and Central Region, increased as compared with 59% in 2019FY. Meanwhile, the aggregated share of Beijing Region and Bohai Rim Region in new land bank dropped to 24% in 2020H1 from 41% in 2019FY. We expect that the shift of strategy could help the Company partially offset its exposure to the regulation risk in a single region in the future.

Fair financial profile and ample liquidity position. As of 30 June 2020, the Company's adjusted debt burden slightly enlarged to RMB89.6 billion by RMB3.5 billion from end-2019. However, its adjusted net gearing ratio reduced to 70.6% from 82.8% over the same period, given cash inflow from property sales. The Company's EBIT interest coverage was 2.3x in 2020H1(LTM). Sino-Ocean maintained an ample liquidity position. As of 30 June 2020, the Company held cash and cash equivalents of RMB43.7 billion, about 2.0x of its short-term debt. Overall, we expect that the Company will maintain a fair net gearing ratio and adequate liquidity position over the next 12-18 months.

Strong shareholder support. The Company is China Life's only platform in real estate sector that has a good track record of receiving support from China Life. In March 2019, the Company and China Life entered into a framework agreement, pursuant to which China Life may, based on its investment needs, subscribe for financial products up to RMB4 billion (or equivalent currencies) per annum from 2019 to 2021 to be issued by the Company through a simplified internal control procedure. This agreement allows China Life to provide financial support to the Company in a timely manner. We expect that the support from China Life is sustainable and is credit positive to the Company.

Proposed spin-off of property management business. On 7 September 2020, Sino-Ocean announced the proposed spin-off and separate listing of Sino-Ocean Services Holding Limited ("Sino-Ocean Service"), a subsidiary engaging in property management services. The spin-off is expected to further improve the Company's as well as Sino-Ocean Services' funding channels, as they can separately gain access to the capital markets. According to the announcement, the Company is expected to retain an interest not less than 50% in Sino-Ocean Services, which the property management business would remain consolidated to the Company's financial profile and provide recurring income to the Company. We will continue to monitor the listing process of Sino-Ocean Services and assess the impact of the spin-off.

Credit Challenges

Depressed contracted sales due to outbreak of COVID-19 and less saleable resources in 2020H1. In 2020H1, the total contracted sales amount of Sino-Ocean dropped by 30.4% YoY to RMB41.8 billion. However, the improvement in cash collection could partially offset the adverse effect from the lower contracted sales. Its cash collection ratio improved to 80% in 2020H1 from 68% in 2019H1, while cash proceeds slightly reduced to RMB33.4 billion from RMB35.7 billion. Sino-Ocean is expected to roll out saleable resources of RMB130 billion in 2020H2, accounting for 65% of its annual resources, which could support its annual contracted sales target of RMB130 billion. However, as the regulatory environment of the property market is expected to remain tight, especially in Bohai Rim Region, Sino-Ocean's contracted sales growth will continue to be under pressure in 2020H2.

Declined net profit margin given decrease in nonrecurring gains. Sino-Ocean's net profit margin reduced from 15.4% in 2019H1 to 10.2% in 2020H1, as its non-recurring gains dropped, including (1) fair value gains on investment properties decreased from RMB375.3 million to losses of RMB22.9 million; (2) other gains decreased from RMB573.0 million to RMB124.5 million (the Company recognized gains from disposing subsidiaries of RMB697.9 million in 2019H1); and (3) profits contributed from joint ventures and associates decreased from RMB923.1 million to RMB224.4 million. We expect that the net profit margin of Sino-Ocean will remain at a relatively low level as compared with its peers over the next 12-18 months.

Rating Outlook

The stable outlook on Sino-Ocean's rating reflects our expectation that the Company would maintain a fair financial profile given its strict investment policy. We also expect that China Life will continue to provide strong support to the Company.

Rating Methodology

The methodology used in this rating is the Rating Methodology for Real Estate Development Industry (December 2019).

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