



CCXAP affirms China SCE Group Holdings Limited's long-term credit rating at BB_g, with stable outlook

Hong Kong, 12 October 2020 -- China Chengxin (Asia Pacific) Credit Ratings Company Limited ("CCXAP") affirms the BB_g long-term credit rating of China SCE Group Holdings Limited ("China SCE" or the "Company"), with stable outlook. China SCE's rating reflects that its fast recovery of contracted sales from the outbreak of COVID-19, as well as its sufficient land bank. However, the rating is also constrained by weakened credit metrics as well as sizable capital expenditure needs for business expansion.

Corporate Profile

Established in 1996, China SCE is one of the fast-growing nationwide property developers in Mainland China. It started its business in Fujian Province and has gradually expanded into other economic zones since 2013, with a presence in 54 cities at mid-2020. In February 2010, it completed the listing on the main board of the Hong Kong Stock Exchange (Stock Code: 1966.HK). As of 30 June 2020, Mr. Wong Chiu Yeung held 50.40% of the Company's shares indirectly via Newup Holdings Limited and was the Company's ultimate controller.

Rating Rationale

Credit Strengths

Growing contracted sales with fast recovery from the disruption of COVID-19 outbreak.

China SCE achieved total contracted sales increased by 8.2% year-over-year ("YoY") to RMB40.1 billion in 2020H1, recovering from a YoY drop of 17.7% in 2020Q1. Supporting by a fast recovery of the Company's contracted sales, its ranking among the Chinese property developers by contracted sales, was upgraded to 37th in 2020H1 from 44th in 2019, according to CRIC. The Company is expected to have total saleable resources of around RMB130 billion in 2020H2 for fulfilling its annual target of RMB93 billion. Among the saleable resources, about RMB85 billion is contributed by newly launched projects, with around 71% in first and second-tier cities. In the first nine months of 2020, the Company reported total contracted sales of RMB69.0 billion, achieving about 74% of its annual target. We expect that the abundant and fairly distributed saleable resources will support the Company to achieve its annual contracted sales target.

Sufficient land bank focusing on second-tier and strong lower-tier cities. As of 30 June 2020, China SCE had a total land bank of 31.2 million sqm, in terms of gross floor area ("GFA"), with average land cost of RMB4,313 per sqm, sufficient to support its contracted sales over the next 3 years. The Company's land bank was mainly in the second-tier (68%) and strong lower-tier cities

(23%) of China, such as Nanjing, Suzhou, and Chongqing, which had relatively solid economic prospects. However, the tightening regulatory environment of property market in second-tier cities could reduce the Company's profit margin. As for regional distribution, Yangtze River Delta accounted for 33% of its total land bank, while the rest were in West Taiwan Strait Economic Zone (27%), Bohai Rim Economic Zone (20%), Central Western Region (14%) and Greater Bay Area (6%).

In 2020H1, China SCE acquired 10 projects with GFA of 3.3 million sqm, at a cost of RMB19.4 billion, equivalent to about 48.5% of the total contracted sales in the same period. Under the "One Body Two Wings" development model, the Company will acquire commercial complexes projects for the development of residential properties as well as shopping malls and long-term rental apartments. Among its newly acquired projects, there were 8 commercial complexes projects, including 6 for the development of shopping malls and 2 for rental apartments. This development model could help the Company replenish land at a lower average cost, which these projects had an average land cost of RMB3,082 per sqm, as compared to its average land cost of RMB4,313 per sqm of its land bank. In addition, residential properties constituted around 84% of the GFA of the commercial complexes (excluding 2 projects in Xuchang City which have not yet been secured), while the rest would be for commercial usage. It is expected that the sales of residential properties could help fund the development of commercial projects, which could partially mitigate the Company's capital expenditure pressure.

Good liquidity buffer. China SCE had an adequate liquidity position as its cash to short-term debt ratio was 1.2x at mid-2020, suggesting that it held enough cash to fulfil its short-term debt obligations. The Company's short-term debt accounted for 45.5% of the total debt at mid-2020, increasing from 29.2% at end-2019 as a larger proportion of debt will mature within a year. Yet, the Company has a good track record of access to capital, which will partially offset its refinancing risk. In July 2020, the Company issued RMB1,460 million onshore corporate bonds at a coupon rate of 5.5% with tenor of 4 years. In addition, the Company drew down offshore syndicated loans of around RMB400 million in July 2020. Overall, we expect that China SCE's refinancing risk would remain manageable over the next 12-18 months.

Credit Challenges

Larger exposure to joint-venture partnership. In 2020H1, the Company's joint ventures and associates contributed 56.3% of total contracted sales, slightly increased as compared to 54.4% in 2019H1. A larger joint-venture exposure could lower China SCE's financial transparency as the financial of joint ventures and associates are not consolidate into the Company's financial statement. Nonetheless, the Company has actively enhanced the equity ownership of its newly acquired projects by holding around 79% of the stakes of new projects acquired in 2020H1, as compared to that of 60% in 2019H1.

Weaker profitability alongside margin compression of property market and decrease in nonrecurring gains. China SCE's gross profit margin reduced to 27.9% in 2020H1 from 28.9% in 2019H1, while net profit margin dropped to 16.6% from 21.1% over the same period. The decline of net profit margin was mainly driven by lower nonrecurring gains, including gains from bargain

purchase and change in fair value of investment properties, which contributed 30.5% of pretax profit in 2020H1, as compared to that of 46.0% in 2019H1. The drops of profitability were within our expectation, which would marginally impair the Company's credit profile. Over the next 12-18 months, we expect that the Company's profitability will compress due to the tight regulatory environment of the property market.

Increase in debt leverage with weakened EBIT interest coverage. The debt burden of China SCE enlarged by RMB3.4 billion to RMB45.5 billion at mid-2020 as compared to 2019 year-end, due to its expansion in operating scale. Its net gearing ratio rose from 60.0% to 68.3% over the same period, but still considered as a moderate level as compared to its peers. The Company's average financing cost retained at around 6.7% at mid-2020. Yet, due to the decline of profitability, its EBIT interest coverage ratio weakened to 2.0x over the last twelve months ended 30 June 2020, as compared to that of 2.5x in 2019H1(LTM). We believe China SCE's interest coverage will remain relatively weak over the next 12 to 18 months owing to margin compression of property market as well as continuous rise in the Company's debt burden.

Rating Outlook

The stable outlook on China SCE's rating reflects our expectation that the Company will maintain a strong market position over the next 12-18 months, underpinned by its sufficient and diversified land bank. We also expect that the Company's good liquidity buffer will help retain its refinancing risk at a relatively manageable level.

Rating Methodology

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

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The first name below is the lead rating analyst for this rating and the last name below is the person primarily responsible for approving this rating.

Jacky Lau

Credit Analyst – Credit Ratings

jacky_lau@ccxap.com

Guo Zhang

Director – Credit Ratings

guo_zhang@ccxap.com

Tel: +852-2860 7111

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China Chengxin (Asia Pacific) Credit Ratings Company Limited

Address: Suites 1904-1909, 19/F, Jardine House,
1 Connaught Place, Central, Hong Kong

Website: www.ccxap.com

Email: info@ccxap.com

Tel: +852-2860 7111

Fax: +852-2868 0656