CCXAP affirms Beijing Capital Land Ltd.'s long-term credit rating at BBB_g-, with stable outlook.

Hong Kong, 31 August 2021 – China Chengxin (Asia Pacific) Credit Ratings Company Limited ("CCXAP") has affirmed the long-term credit rating of Beijing Capital Land Ltd. ("BCL" or the "Company") at BBB_g-. The rating outlook is stable.

The BBB_g- long-term credit rating of BCL is underpinned by the Company's (1) solid track record of receiving ongoing support from its controlling shareholder, Beijing Capital Group Co., Ltd. ("BCG"); (2) good access to projects and funding; and (3) high-quality land bank in top-tier cities in China. However, the rating is also constrained by the Company's (1) geographic concentration particularly in Beijing, making it vulnerable to regional policy risks; (2) weakened profitability; and (3) modest debt leverage and interest coverage.

Corporate Profile

Founded in 2002, BCL (Stock: 2868.HK) is the core property development arm of its parent, BCG, which is a state-owned enterprise wholly owned and directly controlled by the Beijing State-owned Assets Supervision and Administration Commission ("Beijing SASAC"). As of 30 June 2021, BCG is the controlling shareholder of the Company, directly holding 56.7% of its equity interest.

BCL primarily engages in residential and commercial property development projects in China, with geographic focus on the three core metropolitan areas, namely the Beijing-Tianjin-Hebei region, the Yangtze River Delta, and the Guangdong-Hong Kong-Macau Greater Bay Area, as well as other key second-tier cities. BCL also operates outlet business mainly through its Hong Kong-listed subsidiary, Beijing Capital Grand Limited (Stock code: 1329.HK).

Rating Rationale

Credit Strengths

Relatively large operating scale with high-quality land bank in top-tier cities. BCL's total contracted sales amounted to RMB40.3 billion in 2021H1, a moderate increase of 19.5% as compared to the undermined contracted sales in 2020H1 amid the outbreak of COVID-19. With that, its contracted sales to adjusted debt ratio rose slightly to 0.7x in 2021H1(LTM) from 0.6x in 2020H1(LTM). The Company's ranking among the Chinese property developers improved slightly to 55^{th} in 2021H1 from 58^{th} in 2020, by total contracted sales according to CRIC's statistics.

BCL had sufficient high-quality land bank to meet its development needs for the next three years. As of 30 June 2021, BCL had a total land bank of 15.7 million sqm in terms of GFA, of which the attributable land bank to the Company amounted to 10.2 million sqm, covering 31 cities in China. The Company's land reserves are mainly located in top-tier cities with sound economic conditions and strong housing demands. Approximately 84% of the Company's land bank was in top-tier cities, such as Beijing, Wuhan, Tianjin, Kunming, and Chongqing.

BCL slowed down its land bank investment in 2021H1, under the drawback of intense competition in the public auction in top-tier cities. The Company newly acquired 2 projects in Shanghai with a total GFA of 266 thousand sqm at a total cost of RMB3.4 billion, which was equivalent to around 8.4% of contracted sales in 2021H1. In addition, the Company cooperated with Ping An Real Estate to acquire a 50% stake in the Tongxiang High-speed Rail New Town project in January 2021. This project is next to the high-speed rail station, which is a key area in Tongxiang, with a total land area of around 3.5 square kilometers.

Adequate liquidity profile underpinned by good access to funding. As of 30 June 2021, the Company held cash and cash equivalents of RMB38.9 billion, of which restricted cash amounted to RMB2.6 billion. Its cash to short-term debt ratio was 1.4x, suggesting that the Company had enough cash reserve to meet its short-term debt obligations. In addition, the Company has good access to low-cost funding via different financing channels, underpinned by its status as a state-owned enterprise. The Company issued 4 tranches of the onshore corporate bonds of around RMB8.1 billion in 2021H1, with coupon rates ranging between 3.97% and 4.30%. Moreover, the Company raised USD500 million via offshore senior notes with a coupon rate of 4.65%.

Strong shareholder support. BCL's rating reflects our expectation that BCG will provide solid support to BCL when necessary, given that (1) the Company has an important strategic and economic position to its parent, and (2) BCG has a strong track record of providing business and financial support to BCL. BCG is a large state-owned enterprise wholly owned and directly controlled by the Beijing SASAC, with four major business segments including real estate, infrastructure, environmental protection, and financial services. As the core property development arm of BCG, BCL contributed around 40-50% of revenue and net profit to BCG over the past two years. The parental support includes providing access to quality projects, loan guarantee, capital injection and shares subscription, which helps strengthen the overall credit profile of BCL.

On 9 July 2021, the Company announced the proposed privatization and merger, to withdraw its listing on the Hong Kong Stock Exchange, and to be merged into Beijing Capital City Development Group Co Ltd ("Capital Development"), a wholly-owned subsidiary of BCG. Capital Development will pay the cancellation price in cash of approximately HKD5.3 billion for the privatization. After the merger, Capital Development assume all assets, liabilities, interests, businesses, employees, contracts, and all other rights and obligations of the Company. The privatization is mainly driven by the regulatory restrictions on its equity funding. Underpinned by its state-owned background, BCL's financing capability will remain strong in the aspects of access to debt market and bank loans. In addition, we opine that BCG will have more flexibility to support the Company after the privatization. These can largely offset the adverse effect on its financing capability from the privatization. On 18 August, the merger has been approved by the Chinese regulators. The privatization plan is still pending for the approval from the shareholders, and we will continue to monitor the progress.

Credit Challenges

Exposure to geographical concentration and policy risks, despite a slight improvement in diversification. In 2021H1, around 54% of the Company's contracted sales were contributed by the areas outside Beijing-Tianjin-Hebei Region, as compared to 48% in 2020H1. Moreover, the newly acquired land parcels in 2021H1 were all outside the Beijing-Tianjin-Hebei region. However, we opine that the Company's geographical distribution is still relatively concentrated, as Beijing accounted for about 41% of its contracted sales in 2021H1, and about 29% of its land bank was in Beijing and Tianjin at mid-2021. Although Beijing and other top-tier cities have robust housing demands, the strict market regulations on pricing and pre-sales in these cities could weaken the Company's sales performance and profitability.

Exposure to joint-venture projects. In order to fuel its contracted sales growth, BCL has participated extensively in joint-venture projects in the past two to three years. The Company owned 65.1% of the stakes of its total land bank at mid-2021. As of 30 June 2021, the Company provided guarantees of RMB3.9 billion for loans to its joint ventures and associates. BCL's increasing participation in joint-venture projects can help diversify its investment risks and enjoy the synergies from business partners. However, this can also weaken the Company's financial transparency as almost one-third of its projects are excluded from the financial statements.

Deteriorated profitability given tight price restrictions and reduced investment income. The Company's gross profit margin reduced to 20.5% in 2021H1 from 25.3% in 2020H1, of which the gross profit margin of property development slumped from 25.1% to 17.6%. In addition, BCL's investment income (excluding share of profit of joint ventures and associates) declined from RMB1.1 billion in 2020H1 to RMB0.2 billion in 2021H1, which further depressed its profitability. In 2021H1, its net profit margin was 3.8%, declining by 7.2 percentage points YoY. We expect that the intense competition in land auctions and strict price-cap in top-tier cities will continue to weigh on the Company's profitability over the next 12-18 months.

Modest debt leverage and interest coverage. BCL attempted to control its debt growth by moderating its land investments, but its debt burden remained large given its debt-funded expansion and slow inventory turnover. As of 30 June 2021, its adjusted total debt (including perpetual debt and pension debt investment plan) amounted to RMB116.1 billion and net gearing ratio was 270.2%, relatively stable as compared to the end of 2020. BCL's EBIT interest coverage ratio weakened to 0.6x in 2021H1(LTM) from 0.8x in 2020 due to lower profitability. We expect that BCL will actively manage its debt growth through prudent land investment strategy over the next 12-18 months. However, we believe that the Company's high debt leverage will continue to weigh on its stand-alone credit profile over the next 12-18 months, due to its modest business growth prospects and large debt burden.

Rating Outlook

The stable outlook on BCL's rating reflects our expectation that the Company will continue to receive strong support from BCG, given its strategic and economic importance to its parent. We also expect the Company to maintain its debt control and deleveraging progress over the next 12 to 18 months.

What could upgrade the rating?

The rating could be upgraded if the Company (1) demonstrates contracted sales growth and improves its profitability; and (2) ameliorates its credit metrics such as adjusted EBIT/interest ratio increases and net gearing ratio decreases, on a sustained basis.

What could downgrade the rating?

The rating could be downgraded if the Company's (1) strategic position to BCG deteriorates, leading to a weakening of shareholder support; (2) contracted sales and profitability falls materially; or (3) the Company's credit metrics deteriorate, such as cash/short-term ratio falls below 1.0x.

Regulatory Methodology

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

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