Pengyuan International Assigns 'BBB-' Rating to Shimao Property Holdings Limited; Outlook Stable

HONG KONG, 31 January 2019. Pengyuan International has assigned a first-time global scale long-term issuer credit rating (LTICR) of 'BBB-' to Shimao Property Holdings Limited (Shimao). The Outlook is Stable.

Shimao is a Chinese property developer with 96%, 3% and 1% revenue generated from property development, investment property (hotel and rental), and property management as of first half of 2018. Shimao's rating reflects its strong sales execution, high profitability, and diversified and high-quality land bank. On the other hand, Shimao's rating is constrained by its concentrated exposure to China property market and relatively smaller scale measured by revenue.

The Stable Outlook for Shimao reflects Pengyuan International's expectation that the company will keep growing its contracted sales and land bank while maintaining a healthy financial profile.

KEY RATING RATIONALES

Positive

Established homebuilder with high quality land bank. Shimao has built a diversified pan-China homebuilding business that covers 84 cities and a total land bank area of 51.62 million square meter by first half of 2018. Its land reserve life is more than seven years as of first half of 2018. We believe the company's abundant high-quality land bank will support its scale expansion with flexibility in land replenishment.

Strong growth in contracted sales. Shimao has generated strong contracted sales growth of 75% in 2018, following a 48% growth in 2017, with a 76% increase in volume and 1% decline in average selling price (ASP). The sales growth has been supported by the company's execution capability and its land banking strategy. The enlarged scale has helped Shimao to gain market share from the competitors and helped elevate its ranking to No. 11th in 2018 from 16th in 2017, measured by the consolidated contracted sales. Pengyuan International expects Shimao's sales growth to slow to 24% in 2019, because of the market slowdown.

Improving profitability. Despite the industry volatility, Shimao has maintained an EBITDA margin of above 20% in the past ten years. The company has managed to improve its EBITDA margin to 26% in first half of 2018, from 25% in 2017 and 22% in 2016. We expect the company's margin to continue to improve due to the lower land costs, and larger operating scale. In the first half of 2018, Shimao grasped the opportunity of weak land market to replenish its land bank, with ASP for the new land acquired declining 26%. In addition, the investment properties to be launched in 2018-2020 will also widen the company's margin, in our view.

Investment portfolio offers a stable recurring income. Shimao owns a portfolio of high-quality investment properties in tier-1 and tier-2 cities in China. The company targets to complete the Hong Kong hotel and Shenzhen Qianhai office in 2019 after the opening of Shanghai Wonderland Hotel and the repositioning of Shanghai Shimao Plaza in the second half of 2018. We expect Shimao's recurring EBITDA from the investment property to grow 10-15% every year from 2018 to 2020 as a result of its abundant pipeline.

Negative

Concentration risk. Shimao has high exposure to China property market, though its business involves different operations in property. By first half of 2018, property development, hotel, investment property, and property management contributed 96%, 2%, 1% and 1% of its revenue. The company's financial performances are largely influenced by the cyclicality of Chinese economy and its property market.

Smaller scale. Shimao is relatively small measured by revenue, compared to its peers within and outside of the property industry. Shimao reported a revenue of RMB70bn and RMB43bn as of end-2017 and first half of 2018 respectively. We expect its revenue to reach above RMB100bn for the fiscal year of 2018. The company is ranked as top 10 among all the Chinese property developers by three-year average revenue from 2015 to 2017.

Lower efficiencies. Shimao's cash collection rate has decreased to 76% in the first half of 2018 from 80% in 2017, hinting a slower pace of home loan approvals due to the policy control. The lower cash collection, if sustained, is likely to reduce Shimao's cash flow efficiency. Although we believe the impact is likely to be partially mitigated by a higher sell-through.

RATING OUTLOOK

The stable outlook reflects our expectation that Shimao will be able continuously generate a strong growth in contracted sales while maintaining a healthy financial profile.

We would consider downgrading Shimao's issuer credit rating if its credit profile deteriorates substantially, which could be caused by 1) Leverage measured by debt to adjusted inventory increases above 45% on a sustained basis. 2) EBITDA margin falls below 20% on a sustained basis with little recovery prospect. 3) Substantial deterioration of the operating profile.

We would consider upgrading the company's issuer credit rating if its credit profile improves substantially, which could be caused by 1) Improvements of financial profile on a sustained basis. 2) Strengthening of operating profile.

Note: ratings mentioned in this press release are unsolicited ratings.

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Additional information is available on www.pyrating.com

Related Criteria

General Corporate Rating Criteria (15 March 2018)

Industry Credit Guidelines Chinese Homebuilders and Property Developers (31 August 2018)

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