

Lianhe Global has affirmed ‘BB’ global scale Long-term Issuer and Issuance Credit Rating to Yuzhou Group Holdings Company Limited; Issuer Rating Outlook Stable

HONG KONG, 06 November 2020 – Lianhe Ratings Global Limited (“Lianhe Global”), an international credit rating company, has affirmed ‘BB’ global scale Long-term Issuer Credit Rating to Yuzhou Group Holdings Company Limited (01628.HK) (“Yuzhou” or “the company”). The Outlook is Stable.

Lianhe Global has also affirmed ‘BB’ global scale Long-term Issuance Credit Rating to the senior unsecured USD notes issued by Yuzhou. A full list of affirmed issuance ratings is included in this press release.

The Issuer Rating reflects Yuzhou’s established market position in the Chinese property market, which is evident by its strong contracted sales growth, increasing in high-quality land bank primarily located in tier 1 and 2 cities in China, and healthy margins. However, Yuzhou’s rating is constrained by its elevated financial leverage as compared with its peers.

The Stable Outlook reflects our expectation that Yuzhou would continuously expand its operating scale through measured land acquisitions to sustain its contracted sales growth, particularly on a consolidated basis, while reasonably managing its debt growth and stable margins.

Key Rating Rationales

Quality Land Bank with Increasing Focus on Project Consolidation: Yuzhou had a total land bank of 20.24 million square meters (sq.m.) at end-June 2020, primarily in the Yangtze River Delta Region, Bohai Rim Region, and West Strait Economic Zone, with a majority located in tier 1 and tier 2 cities in terms of saleable resources. The company has also been expanding its geographic coverage beyond its home base by including some satellite cities in coastal regions.

In the first eight months of 2020, Yuzhou acquired a total of 15 new land parcels totaled 2.57 million sq.m. (attributable 1.66 million sq.m.), all of which are located in tier 1 and tier 2 cities, which were in-line with the company’s strategic focus in the last 18 months on addition to land banks from higher-tier cities. As a result, Yuzhou’s average land cost increased from c. RMB5,000 per sq.m. in 2018, to c. RMB10,023 per sq.m. in 2019 and c. RMB12,216 per sq.m. in the eight months ended August 2020. The company utilized a balanced approach in land purchase with approximately the same split between bidding and auction vs. mergers and acquisitions. We believe Yuzhou’s rising land cost could be compensated by higher average selling prices (ASP) of its quality land bank of higher-tier cities, as evidenced by the year-over-

year increase in ASP for the nine months ended September 2020. We expect the ASP of the company's project to record an average annual increase of c.5% in the next 12-18 months.

Yuzhou was focusing on using joint ventures and associates in order to substantiate its sales growth, which inevitably gave rise to concerns on financial transparency due to the off-balance-sheet nature of these partnerships. We expect Yuzhou to gradually increase its focus on project consolidation, as seen from a larger portion of land acquired in the first eight months of 2020 would be consolidated. Over 40%, in terms of gross floor area (GFA), of the 15 land parcels, is 100% owned by the company. Yuzhou's land bank is sufficient for development for 2-3 years, and therefore we expect Yuzhou will need to continue to replenish its land bank in a measured manner to keep up with its sales and growth plan.

Strong Execution Capability Leading to Expanding Sales Scale with Stable Margins:

Yuzhou reported contracted sales of RMB42.9 billion for 1H 2020 and RMB77.1 billion for the nine months ended September 2020, representing 42.9% and 77.1% of the full-year target of RMB100 billion, respectively. Contracted sales in 1H 2020 and for the nine months ended September 2020 represented an increase of 50.5% and 57.7%, respectively, on a year-over-year basis. The prominent sales growth demonstrated Yuzhou's execution capability under the backdrop of the COVID-19. The strong sales growth enables the company to expand its scale in terms of both revenue and land bank.

At end-June 2020, Yuzhou had RMB116 billion of saleable resources scheduled for 2H 2020, with over 60% were located in the Yangtze River Delta Region, which still presented relatively resilient fundamentals in the property markets. We believe Yuzhou is on track to meet its full-year target of RMB100 billion, and will slow down its pace of sales growth to c.10-15% per annum in the next 12-18 months to focus more on improving profitability and financial performance instead.

Given the restrictions on home prices and rising land cost in higher-tier cities, especially tier 2 cities, we have seen some margin squeezing for Yuzhou. The company has been aiming to maintain a managed expansion pace and targeted land acquisition strategy with a goal to maintain margins. Yuzhou had c. RMB45 billion worth of unrecognized contracted sales on a consolidation basis at end-June 2020, a majority of which will be booked in the next one to two years. We expect the company to maintain a stable gross margin of c. 26-28% in the next 12-18 months, a level considered to be decent vis-à-vis industry average, as the unrecognized contracted sales carry a similar gross margin mix and as the company strategically replenishes its land bank.

Elevated Yet Stabilizing Financial Leverage with Healthy Maturity Profile:

Yuzhou's financial leverage was relatively high as measured by its debt/capitalization ratio of 70.1% at end-2019. As Yuzhou replenished more land at higher costs in 2019 and 1H 2020 compared with the previous years, which was partially funded by debt, its reported debt level increased to RMB62.7 billion at end-June 2020 from RMB54.4 billion at end-2019 and RMB43.6 billion at end-2018. On the other hand, guarantees in relation to joint ventures and associates came

down from RMB12.4 billion at end-2019 to RMB7.9 billion at end-June 2020, which partially helped in stabilizing Yuzhou's financial leverage.

In the first eight months of 2020, Yuzhou spent a total of RMB31.2 billion on land acquisition, representing c. 31% of the company's full-year total sales target of RMB100 billion. As Yuzhou continues to maintain a target spending of 50% or less from the total contracted sales on land acquisition, we expect the company to manage its debt growth in tandem with its contracted sales growth and acquire lands selectively.

Yuzhou has been extending its debt maturity profile in order to mitigate short-term re-financing stress. In addition, Yuzhou's liquidity is adequate as it had RMB43.0 billion (RMB40.7 billion unrestricted) cash on hand and c. RMB46 billion undrawn committed credit facility at end-June 2020 to cover its RMB21.0 billion of debt maturing within 12 months and committed land premium of RMB2.2 billion.

Rating Sensitivities

We would consider downgrading Yuzhou's rating if it were to aggressively replenish its land bank which results in an increase in its financial leverage as measured by debt/capitalization to over 75% or a decrease in its EBITDA interest coverage to below 2.5x consistently, and/or its operating performance were to experience a material deterioration or liquidity position is worsened.

We would consider upgrading Yuzhou's rating if it were to (1) sustain growth both in scale and diversity, and (2) maintain its financial leverage as measured by debt/capitalization at below 60% and EBITDA interest coverage at above 4.5x consistently.

Any rating action on Yuzhou's rating would result in a similar rating action on the USD notes.

Full List of Issuance Ratings

- USD500 million 8.625% senior unsecured notes due 2022 affirmed at 'BB'
- USD500 million 8.500% senior unsecured notes due 2023 affirmed at 'BB'
- USD500 million 8.500% senior unsecured notes due 2024 affirmed at 'BB'
- USD500 million 8.375% senior unsecured notes due 2024 affirmed at 'BB'
- USD500 million 8.300% senior unsecured notes due 2025 affirmed at 'BB'
- USD645 million 7.375% senior unsecured notes due 2026 affirmed at 'BB'

About Lianhe Global

Lianhe Global is an international credit rating company that provides credit ratings to corporations, banks, non-bank financial institutions, local government financing vehicles, and other asset classes around the globe. Lianhe Global also provides credit risk research and other services related to credit ratings.

Rating Methodology

The principal methodology used in this Yuzhou's rating is Lianhe Global's General Corporate Rating Criteria published on 16 July 2018 which can be found at the website www.lhratingsglobal.com.

Note: The above Issuer/Issuance Credit Ratings are solicited at the request of the rated entity or a related third party.

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