

Credit Opinion

21 August 2024

Ratings	
Category	Financial Institution
Domicile	China
Rating Type	Solicited Rating
Long-Term Credit Rating	A _g -
Outlook	Stable

Analyst Contacts

Vincent Tong +852-2860 7125
Assistant Director of Credit Ratings
vincent_tong@ccxap.com

Christy Liu +852-2860 7130
Credit Analyst
christy_liu@ccxap.com

Elle Hu +852-2860 7120
Executive Director of Credit Ratings
elle_hu@ccxap.com

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

Client Services

Hong Kong +852-2860 7111

Zhongyuan Aviation Leasing Co., Ltd.

Initial credit rating report

CCXAP assigns first-time long-term credit rating of A_g- to Zhongyuan Aviation Leasing Co., Ltd., with stable outlook.

Summary

The A_g- long-term credit rating of Zhongyuan Aviation Leasing Co., Ltd. ("ZYAL" or the "Company") is underpinned by the Company's (1) solid leasing business development in Henan Province; (2) stable asset quality; and (3) good capital adequacy.

However, the rating is constrained by (1) weakened operating environment for leasing companies due to tightening regulations and economic slowdown; (2) ZYAL's small operating scale and modest profitability; and (3) concentrated asset portfolio.

The rating also reflects our expectation of a high likelihood of support from its key shareholder, namely, Zhongyuan Asset Management Co., Ltd. ("Zhongyuan AMC"), given the Company's (1) strong strategic status as the core leasing subsidiary of Zhongyuan AMC; (2) moderate operational and management linkage with Zhongyuan AMC; and (3) high reputation risk to Zhongyuan AMC. We believe that Zhongyuan AMC has strong capacity to support as the largest local AMC in Henan Province which is ultimately controlled by the Finance Department of Henan Province.

The stable outlook on ZYAL's rating reflects our expectation that the Company, as the core leasing subsidiary role in the group, will remain its operational linkage with Zhongyuan AMC. We also expect ZYAL will sustain its business position and financial profile over the next 12 to 18 months.

Rating Drivers

- Weakened operating environment due to tightening regulations and economic slowdown
- Solid leasing business development in Henan Province
- Stable asset quality while having concentration risk
- Small operating scale and modest profitability
- Good capital adequacy and moderate asset liquidity
- High likelihood of support from the key shareholder

Rating Sensitivities

What could upgrade the rating?

The rating could be upgraded if (1) the likelihood of support from Zhongyuan AMC is expected to be stronger such as increase in legal or operational linkage with Zhongyuan AMC; (2) the Company materially improves its profitability and capital base; and (3) the Company further diversifies its asset portfolio with enhanced quality.

What could downgrade the rating?

The rating could be downgraded if (1) the credit quality of Zhongyuan AMC deteriorates or shareholder support is expected to be weakened; (2) the Company demonstrates a material decline in asset quality, such as surging problem assets and impairment losses; or (3) the Company has severely weakened asset-liability management and liquidity position.

Key Indicators

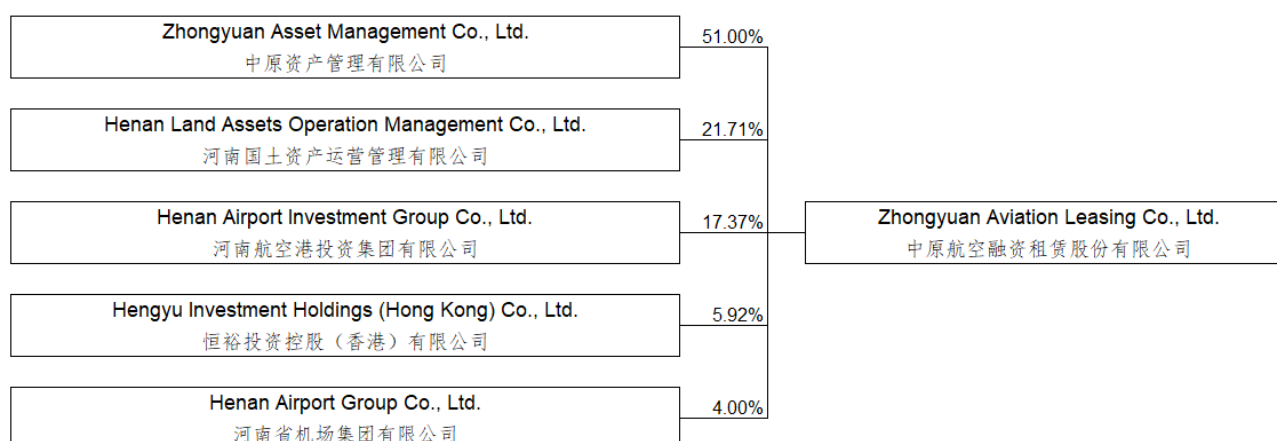
	2021FY	2022FY	2023FY
Total Assets (RMB billion)	7.3	6.6	7.1
Total Equity (RMB billion)	1.9	1.9	2.5
Total Revenue (RMB billion)	0.6	0.6	0.5
Net Profits (RMB billion)	0.2	0.1	0.2
Pre-Tax Net Income/Average Assets (%)	3.1	2.6	3.2
Return on Equity (%)	8.7	7.1	7.5
Realizable Assets/Short-Term Debt (%)	25.2	18.2	34.0
Asset Impairment/Tangible Assets (%)	0.0	1.4	-0.4
Problem Loans/Net Loans (%)	0.0	0.0	0.0

All ratios and figures are calculated using CCXAP's adjustments.

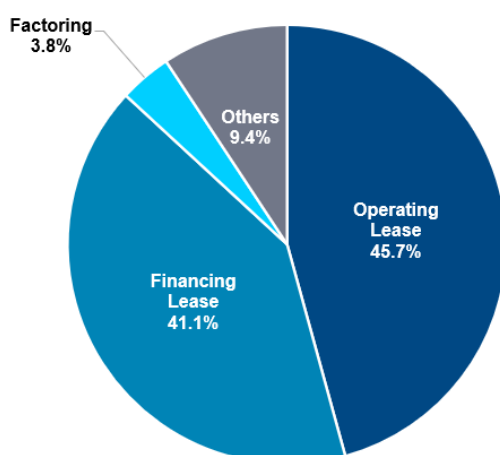
Source: Company data, CCXAP research

Corporate Profile

Founded in 2016, ZYAL is a leasing company located in Henan Province that dedicates to support the development of the local aviation industry. The Company adopts a “finance + industry” business development model and provides comprehensive financing services to its clients, covering operating and financial leasing, commercial factoring, and residual value processing. With years of experience and its professional team specializing in aircraft business, ZYAL has gained a good market position in Henan Province. As of end-2023, the Company had a total asset of RMB7.1 billion and a net asset of RMB2.5 billion. Zhongyuan AMC is the largest shareholder of ZYAL that directly held 51% of the Company's shares, as of end-2023.

Exhibit 1. Shareholding chart as of 31 December 2023

Source: Company information, CCXAP research

Exhibit 2. Revenue structure in 2023

Source: Company information, CCXAP research

Rating Considerations**Weakened operating environment due to tightening regulations and economic slowdown**

Finance leasing is another financing solution besides obtaining loans from lending institutions. Over the past years, Chinese leasing companies have offered corporate customers more flexible and cost-effective financing solutions, particularly for small and medium-sized enterprises (“SMEs”) with limited access to traditional lending institutions. The sector is now under a stricter regulatory environment as the China Banking and Insurance Regulatory Commission (“CBIRC”) has become the regulator for all Chinese finance leasing companies since April 2018, which was previously regulated by the Ministry of Commerce. The CBIRC issued various regulation policies, such as the “*Interim Measures for the Supervision and Administration of Financial Leasing Companies*” (融资租赁公司监督管理暂行办法) in June 2020 and “*Regulations on off-site Supervision of Financial Leasing Companies*” (融资租赁公司非现场监管规程) in February 2022. In addition, several provincial-level cities have successively introduced regulatory implementation rules for financing leasing companies. We believe that the tightening regulations will improve the regulatory framework for the industry, strengthen the supervision of leasing companies, and reduce the chance of market crunches in the long run. However, the regulatory change

also requires a higher standard of management and internal control for financial leasing companies and increases their management pressure.

The business development of ZYAL is closely related to China's economic changes and leasing industry. The financial leasing market in China is under a contraction since 2020 owing to tightening policies and unfavorable market environment, which is expected to further intensify market competition. As of 31 March 2024, the outstanding financial leasing contracts in China decreased by 0.4% to RMB5.6 trillion compared to that at end-2023. In addition, the global pandemic situation from 2020 to 2022 has brought negative impacts on the operation of the aviation transport market. The main operating indicators of the civil aviation industry such as total transport turnover and passenger turnover have declined significantly during the pandemic, restricting ZYAL from business expansion and giving pressure on its customers. Fortunately, the aviation transport market has gradually recovered after 2023, which may drive up the demands in aircraft leasing market and improve the credit quality of airline companies. However, the ascending rivalry in the financial leasing market is still expected to challenge small-to-medium size lessors, including ZYAL.

Solid leasing business development in Henan Province

ZYAL has established a solid market position in Henan Province as the first comprehensive financial leasing company with geographic advantages. It dedicates to support the development of the local aviation industry development and has played an important role in the finance resources of Zhengzhou Airport Economic Comprehensive Experimental Zone's construction and development. Given its strong state-owned shareholder background and its own business resources, the Company has developed its market competitiveness in both operating leasing and financial leasing businesses in Henan Province. The Company also widens its service offerings to include commercial factoring in order to satisfy its clients' needs and enlarge its business scale. ZYAL's customers cover large state-owned enterprises, airline operators, utilities providers, and leading private-owned enterprises in different sectors.

The Company has a stable operating lease asset portfolio, including aircrafts and real estate properties. As of end-2023, the Company had 7 aircrafts with young ages of 6 to 8 years. These aircrafts are leased out to medium to large airlines including China Eastern Airlines Co, Ltd., Xiamen Airlines Co., Ltd., and Hebei Airlines Co., Ltd., with lease terms from 8 to 15 years. The Company also has two office buildings in Zhengzhou City, with a total construction area of around 38,747 square meters. The office buildings are leased to large state-owned enterprises, well-known private-owned enterprises, domestic financial institutions, and large hotel chains, with a high occupancy ratio of above 90%. Financial leasing business is also one of the core businesses of the Company. However, the outstanding amount of its financial leasing assets dropped 7.5% YoY to RMB2.6 billion as of 31 December 2023, given stricter regulatory policies and slowdown on new investments. Its financial leasing business is mainly under sale-and-leaseback model.

ZYAL started its commercial factoring business in 2022 through its subsidiary. It mainly develops factoring business around bulk commodities, engineering construction, and high-quality leasing customers in Henan Province. As of end-2023, the Company had outstanding factoring receivables of RMB173.3 million, all of which were recourse factoring.

Stable asset quality while having concentration risk

ZYAL's asset quality is relatively good. As of end-2023, the Company had no non-performing asset for its financial leasing and factoring businesses. The special mention assets only accounted for 1.7% of its outstanding financial leasing assets. The financial leasing assets included a wide range of items, including

machinery and equipment, automobiles, and buses. However, we believe that the Company's asset quality is still undermined by China's broad economic slowdown. There could be operating and financial challenges for its clients and, in turn, adversely affect its asset quality.

Additionally, ZYAL has demonstrated geographical and sector concentration its financial leasing portfolio. More than 90% of financial leasing assets are concentrated within Henan Province, which may expose ZYAL to the risk of economic and policy changes of a single sector or region. ZYAL also has concentrated financial leasing asset portfolios in urban public utility projects, such as government-enterprise cooperation sector, which is subject to higher policy and regulatory risk. The Company is adjusting its investment strategy to reduce its exposure to this sector and increase its diversification by lowering the amount on each leasing contract. As of end-2023, government-enterprise cooperation sector accounted for 25.4% of its total financial leasing assets, followed by manufacturing (19.2%), leasing & business service (18.2%), and electricity, heat, gas and water production and supply (11.5%). The clients in the urban public utility sector includes urban infrastructure construction, urban operation and municipal services, which mainly consist of local infrastructure investment and financing companies ("LIIFCs") and other state-owned enterprises. The sector concentration risk could be mitigated by ZYAL's diversified client base. The largest single client accounted for around 9.5% of its total financial leasing asset as of end-2023. As the Company still focuses its business on Henan Province under the government's guidance, we expect that the Company's geographic concentration will remain high in the next 12-18 months.

Small operating scale and modest profitability

ZYAL's asset and capital scale remain relatively small, which may disadvantage its ability to withstand the changing environment and grab new business opportunities. As of end-2023, the Company had a total asset of RMB7.1 billion and a net asset of RMB2.5 billion, which is relatively low compared with other medium-size Chinese lessors. The profitability of ZYAL was also modest as seen by its low level of average ROE ratio of 7.8% over the past three years. The limited earnings generation may reduce its buffer in a stressed market environment or to stay competitive with other contenders. ZYAL's modest profitability is partly driven by its narrowed spread in its financial and operating leasing business and the decreasing scale in financial leasing assets. ZYAL's total revenue decreased from RMB615.5 million in 2021 to RMB533.6 million in 2023, mainly arising from the declining scale of financial leasing business. Its net profit slightly increased from RMB162.3 million in 2021 to RMB164.7 million in 2023. We expect the ZYAL's profitability to be modest over the next 12 to 18 months, given that it persists in its prudent investment strategy and intense market competition.

Good capital adequacy and moderate asset liquidity

The Company has a good capital adequacy because of capital injection from its shareholders. Its capital base increased to RMB2.5 billion as of end-2023 from RMB1.9 billion as of end-2021. The capital adequacy ratio, calculated as net capital to total assets, was recorded at 35.0% as of end-2023. In addition, ZYAL's debt leverage is generally lower than that of most companies in the leasing industry. Over the last three years, its capitalization ratio (total debt/total equity) remained above 60%. As of end-2023, the Company had a total debt of RMB4.2 billion. ZYAL's debt financing mainly comes from bank loans, which accounted for more than 60% of its total debt.

The Company maintains moderate asset-liability management with a certain duration mismatch. Around half of the Company's leasing and loan receivables matured within 1 year, while the short-term debt less than 1 year accounted for around 64.2% of its debt profile. The Company also matches the aircraft assets in the operating lease business with debts of more than 5 years. In addition, ZYAL's liquidity buffer is moderate given its low

level of liquid assets. As of end-2023, the Company had realizable assets of RMB924.5 million, which only accounted for approximately 34.0% of its short-term debt. As of year-end 2023, the secured debt/tangible assets ratio was moderate, at 23.2%.

The weak liquidity position could be partly mitigated by its standby liquidity cushion, with total bank facilities of RMB8.1 billion and available bank facilities of RMB4.0 billion as of 31 March 2024. The credit facilities are provided by large domestic banks, such as Export-Import Bank of China, Bank of China, and China Bank of Communications. The Company also had access to different financing products.

External Support

High likelihood of support from Zhongyuan AMC

We expect ZYAL to receive support from Zhongyuan AMC in times of need. This expectation incorporates our considerations of the Company's (1) status as the core leasing subsidiary of Zhongyuan AMC; (2) moderate operational and management linkage with Zhongyuan AMC; and (3) high reputation risk to Zhongyuan AMC.

Zhongyuan AMC was the first local distressed AMC in Henan Province and the only local AMC under the direct management of the Finance Department of Henan Province. It is one of the key provincial financial platforms of Henan Province and undertakes the strategic role of resolving regional financial risk and promoting the upgrade of local industries in the province. ZYAL is the core leasing subsidiary of Zhongyuan AMC under Zhongyuan AMC's development blueprint.

Zhongyuan AMC maintains a moderate degree of control over ZYAL's operations, including the formulation of business strategies and the nomination of the board of directors and key management personnel. The Company is also required to report its annual budget, objectives, plans, and performance to Zhongyuan AMC. ZYAL receives good support from Zhongyuan AMC, given its regional importance in the development of the aviation industry in Henan Province. In 2023, ZYAL received a capital injection of RMB500 million from its shareholders, including a cash injection of RMB255 million from Zhongyuan AMC. As one of the core subsidiaries of Zhongyuan AMC, we expect Zhongyuan AMC to provide ongoing support to the Company, which is unlikely to change in the near to medium term.

Rating Methodology

The methodology used in this rating is the Rating Methodology for [Finance Companies \(April 2019\)](#).

Copyright © 2024 China Chengxin (Asia Pacific) Credit Ratings Company Limited ("CCXAP"). All rights reserved.

No part of this publication may be reproduced, resold, or redistributed in any form or by any means, without prior written permission of CCXAP.

A credit rating is the analytical result of current credit worthiness and forward-looking opinion on the credit risk of a rated entity or a debt issue. Credit ratings issued by CCXAP are opinions on the current and relative future credit risk of the rated entities or debt issues, but do not address any other risks, including but not limited to liquidity risk, market price risk, and interest rate risk.

Credit ratings, non-credit assessments, and other opinions included in CCXAP's publications are not recommendations for investors to buy, sell, or hold particular securities, nor measurements of market value of the rated entities or debt issues. While obtaining information from sources it believes to be reliable, CCXAP does not perform audit and undertakes no duty of independent verification or validation of the information it receives from the rated entities or third-party sources.

All information contained herein belongs to CCXAP and is subject to change without prior notice by CCXAP. CCXAP considers the information contained herein to be accurate and reliable. However, all information is provided on an "as is" and "as available" basis and CCXAP does not guarantee accuracy, adequacy, completeness, or timeliness of the information included in CCXAP's publications.

To the extent where legally permissible, CCXAP and its directors, officers, employees, agents and representatives disclaim liability to any person or entity (i) for any direct or compensatory losses or damages, including but not limited to by any negligence on the part of, and any contingency within or beyond the control of CCXAP or any of its directors, officers, employees, agents or representatives, arising from or in connection with the information contained herein or the use of or inability to use any such information; and (ii) for any indirect, special, consequential, or incidental losses or damages whatsoever arising from or in connection with the information contained herein or the use of or inability to use any such information, even if CCXAP or any of its directors, officers, employees, agents or representatives is advised in advance of the possibility of such losses or damages.

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