

Credit Opinion

4 September 2023

Ratings	
Senior Unsecured Debt Rating	BBB _g +
Long-Term Credit Rating	BBB _g +
Outlook	Stable
Category	Corporate
Domicile	China
Rating Type	Solicited Rating

Analyst Contacts

George Wang +852-2860 7134
Credit Analyst
george_wang@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

Xi'an Kingfar Holding (Group) Co., Ltd.

Initial credit rating report

CCXAP assigns first time long-term credit rating of BBB_g+ to Xi'an Kingfar Holding (Group) Co., Ltd., with stable outlook.

Summary

The BBB_g long-term credit rating of Xi'an Kingfar Holding (Group) Co., Ltd. ("XKFH" or the "Company") reflects (1) the government of Xi'an Economic and Technological Development Zone's ("Xi'an ETDZ") strong capacity to provide support; and (2) the local government's extremely high willingness to provide support, based on our assessment of the Company's characteristics.

Our assessment of Xi'an ETDZ Government's capacity to provide support reflects Xi'an ETDZ's status as one of the national-level development zones with sound industrial fundamentals and good economic and fiscal stability, but constrained by its high debt burden and moderate refinancing environment.

The rating also reflects the local government's willingness to provide support, which is based on the Company's (1) essential role as the comprehensive urban developer and operator in Xi'an ETDZ; (2) solid track record of receiving government support; and (3) good access to funding.

However, the Company's rating is constrained by its (1) medium exposure to commercial activities with high proportion in the property development segment; and (2) high debt leverage and increasing refinancing pressure.

The stable outlook on XKFH's rating reflects our expectation that Xi'an ETDZ Government's capacity to provide support will remain stable, and the Company will maintain its essential role as the comprehensive urban developer and operator in Xi'an ETDZ over the next 12-18 months.

Rating Drivers

- Essential role as the comprehensive urban developer and operator in Xi'an ETDZ
- Medium exposure to commercial activities with high proportion in the property development segment
- Solid track record of receiving government support
- High debt leverage and increasing refinancing pressure
- Good access to funding and concentrated on bank loans

Rating Sensitivities

What could upgrade the rating?

The rating could be upgraded if (1) Xi'an ETDZ Government's ability to provide support strengthens; and (2) the Company's characteristics change in a way that strengthens local government's willingness to provide support, such as improved debt management and liquidity position.

What could downgrade the rating?

The rating could be downgraded if (1) Xi'an ETDZ Government's ability to provide support weakens; or (2) the Company's characteristics change in a way that decreases the local government's willingness to provide support, such as reduced regional significance, materially increased exposure to commercial activities, or further deteriorated liquidity position.

Key Indicators

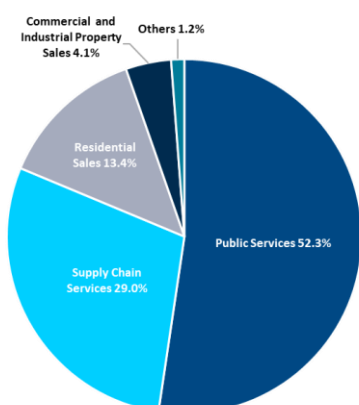
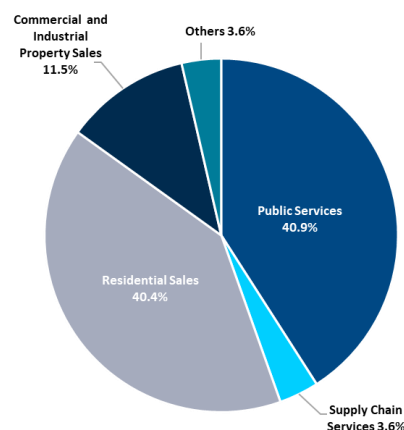
	2020FY	2021FY	2022FY	2023Q1
Total Asset (RMB billion)	49.1	61.1	70.5	73.6
Total Equity (RMB billion)	13.0	14.8	19.2	19.1
Total Revenue (RMB billion)	6.0	7.1	9.6	1.8
Total Debt/Total Capital (%)	66.1	72.7	67.8	69.5

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

Source: CCXAP research

Corporate Profile

Founded in 2010, XKFH is the most important local infrastructure investment and financing company ("LIIFC") of Xi'an ETDZ, which is positioned as a comprehensive state-owned assets management entity. XKFH is mainly responsible for urban construction and management, and provision of public services in the core area of Xi'an ETDZ and has gradually expanded its businesses in recent years. The Company is also engaged in diversified commercial activities, such as property development, property leasing, property management, supply chain services, equity investment, as well as financial services. As of 31 March 2023, the Company was directly and wholly owned by the Management Committee of Xi'an ETDZ. Xi'an ETDZ Government is the ultimate controller of the Company.

Exhibit 1. Revenue structure in 2022**Exhibit 2. Gross profit structure in 2022**

Source: Company information, CCXAP research

Exhibit 3. Shareholding chart as of 31 March 2023

Source: Company information, CCXAP research

Rating Considerations

Government's Capacity to Provide Support

We believe that the Xi'an ETDZ Government has strong capacity to provide support for the Company, given Xi'an ETDZ's status as one of the national-level development zones with sound industrial fundamentals and good economic and fiscal stability, but constrained by its high debt burden and moderate refinancing environment.

Xi'an City is the provincial capital of Shaanxi Province and is located in the center of Shaanxi Province. It is also a Vice-provincial City and a National Central City approved by the State Council. On the back of its geographical advantages, Xi'an City has developed six pillar industries, including electronic information manufacturing, automobiles, aerospace, high-end equipment manufacturing, new materials and new energy, as well as biomedicine. Xi'an City is the biggest city in Shaanxi Province in terms of economic size and its gross regional products ("GRP") ranked first in Shaanxi Province over the past five years. In 2022, Xi'an City reported GRP of over RMB1.1 trillion, representing a year-over-year ("YoY") growth of 4.4% and accounting for approximately 35% of Shaanxi Province's GRP. It also has good fiscal stability with tax income contributing to over 70% of the general budgetary revenue over the past three years. However, its fiscal balance ratio (calculated by general budgetary revenue/general budgetary expenditure) was 53.0% in 2022, which was at a relatively weak level. Xi'an City also had a relatively high debt burden as its outstanding government debt was RMB362.6 billion as of 31 December 2022, accounting for 31.6% of its GRP.

Exhibit 4. Key economic and fiscal indicators of Xi'an City

	2020FY	2021FY	2022FY
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GRP (RMB billion)	1,002.0	1,068.8	1,148.7
GRP Growth (%)	5.2	4.1	4.4
General Budgetary Revenue (RMB billion)	72.4	85.6	83.4
General Budgetary Expenditure (RMB billion)	134.8	147.5	157.3
Local Government Debt (RMB billion)	281.0	323.1	362.6

Source: Statistics Bureau of Xi'an City, CCXAP research

Formed in 1993, Xi'an ETDZ was approved as a national-level development zone by the State Council in 2000, a national-level export processing zone in 2002, the economic and development functional zone of China (Shaanxi) Pilot Free Trade Zone in 2017. With the rapid development in recent years, Xi'an ETDZ has formed eight industrial clusters, including automobiles, high-end equipment manufacturing, military-civilian integration, headquarters economy and modern financial industry, consumer goods manufacturing, strategic emerging industries, modern service industry, and energy processing industry. Xi'an EDTZ has attracted various Fortune 500 companies, listed companies, and large state-owned enterprises to settle in.

Supporting by its solid industrial base, Xi'an EDTZ shows stable economic growth and relatively strong fiscal performance. From 2020 to 2022, Xi'an EDTZ's GRP was RMB89.5 billion, RMB103.2 billion, and RMB112.5 billion, respectively. Its GRP ranked 2nd among all development zones in Xi'an City. Xi'an EDTZ's general budgetary revenue reduced from RMB4.1 billion in 2020, RMB4.7 billion in 2021 to RMB3.7 billion in 2022, mainly due to the impact of tax rebates. Nevertheless, Xi'an EDTZ has had stable revenue sources as taxes accounted for more than 85% over the past years. Meanwhile, Xi'an EDTZ's fiscal balance was relatively high as the self-sufficiency rate (general budgetary revenue/general budgetary expenditure) was 78.3% in 2022. As of end-2022, Xi'an EDTZ's outstanding government debt amounted to RMB6.7 billion, accounting for about 5.9% of GRP. However, Weibei New City, the largest of the four major development areas in Xi'an ETDZ, has a heavy debt burden and negative public opinion, which may hinder the region's refinancing environment.

Exhibit 5. Key economic and fiscal indicators of Xi'an ETDZ

	2020FY	2021FY	2022FY
GRP (RMB billion)	89.5	103.2	112.5
GRP Growth (%)	3.0	10.9	6.5
General Budgetary Revenue (RMB billion)	4.1	4.7	3.7
General Budgetary Expenditure (RMB billion)	3.8	5.9	4.7
Local Government Debt (RMB billion)	7.1	6.8	6.7

Source: Statistics Bureau of Xi'an ETDZ, CCXAP research

Government's Willingness to Provide Support

Essential role as the comprehensive urban developer and operator in Xi'an ETDZ

XKFB has become the most important LIIFC and plays an essential role in urban infrastructure and operation of public utilities in Xi'an ETDZ, after the consolidation of several subsidiaries since 2018. The Company is mainly responsible for urban construction and management, and provision of public services, such as urban municipal engineering operation and maintenance, water and heat supply, urban cleaning, as well as cultural education.

As the major developer and operator of Xi'an ETDZ, XKFB mainly participates in the construction of various types of infrastructure facilities in Xi'an ETDZ, including road infrastructure construction, landscaping, and pipeline construction. Benefiting from the state-owned background with complete construction qualifications,

the Company usually obtains high-quality projects through agency construction and management by the government parties or market-based bidding. Among them, the infrastructure projects mainly undergoes engineering construction through different type of models, such as self-operated, associated management, and agency management. The project is settled according to the construction progress, and generally receives payments within a short time after the completion. As of 31 March 2023, the Company had completed nearly 30 key projects, with total investment of RMB3.2 billion and repayments of RMB1.5 billion. All projects are expected to achieve full payment by 2025. There are also sufficient project reserves and the business sustainability is strong. At the same time, the Company had 15 projects under construction and 8 projects under planning, with total estimated investment amount of RMB1.8 billion and uninvested amount of RMB568.2 million. Such projects are essential to the sustainable development of Xi'an and are beneficial to the local livelihood.

XKFH also undertakes urban operations such as water supply and heating business through several subsidiaries in some areas of Xi'an ETDZ. The Company engages in heat supply using natural gas, mainly providing heat to industrial parks in Xi'an ETDZ at government-set prices, among which the Jinghe Industrial Park is the main one. As of 31 March 2023, the Company had an hourly steam production capacity of 394 tons. XKFH is responsible for the water supply of Jinghe Industrial Park and Jinghe New City, including domestic water and industrial water. The Company owns one water plant with a total annual water supply capacity of 10.95 million cubic meters. However, the subsidiary engaging in water supply has been transferred to other state-owned enterprises in June 2023 due to the water supply and drainage integration policy in Xi'an City, and the Company will no longer take part in this business.

Moreover, XKFH is engaged in urban cleaning and park management in Xi'an ETDZ, of which the cleaning business mainly involves the cleaning of the municipal roads and the daily sanitation and management of the 114 free public toilets in the region. Overall, as the most important entity in the urban construction and operation of Xi'an ETDZ through providing comprehensive public services, we expect that the Company's monopoly position will be maintained in the foreseeable future given the sustainability of its policy-related business.

Medium exposure to commercial activities with high proportion in the property development segment

XKFH is also engaged in diversified commercial activities, such as property development, property leasing, property management, supply chain services, equity investment, as well as financial services. While commercial activities generate supplemental income, they may also pose higher operational and business risks. We consider the Company's exposure to commercial businesses be medium, although accounting for more than 30% of its total assets as of 31 December 2022, as some businesses such as industrial property development, equity investment, and financial services are policy-driven and aim to promote local development.

XKFH actively engages in property development business in Xi'an ETDZ and expands to New Town and Xixian New Area, including construction of commercial housing, office buildings, industrial parks, and factory buildings, generating income through sales or leasing. The Company relies on its own funds and external financing for project construction and the balance of project funds depends on the subsequent lease and sale. As of 31 March 2023, the Company had completed number of property development projects, with a total constructed area of 3397.3 thousand square meters, most of which had been sold. The Company also had 10 projects under construction and planning, with a total investment of RMB23.0 billion and an outstanding amount of RMB13.6 billion. However, since the Company's property sales are easily affected by the market conditions, together with large initial and future investments, the cash collection and investment return are uncertain.

Leasing and property management services also provide stable income to the Company, the majority are operated under the guidance of the local government. XKFH has carried out property management services for

the properties it has constructed. As of 31 March 2023, the Company had 172 property management projects, with a total management area of 14.3 million square meters. The Company has also constructed number of properties for leasing, including office buildings, industrial parks, factory buildings, and apartment houses. As of 31 March 2023, the Company owned more than 30 properties for leasing, with an average occupancy rate of over 75%. Meanwhile, the Company still had 3 key industrial parks under construction and planning, with a total investment of RMB2.5 billion and an outstanding amount of RMB1.6 billion, exerting higher investment pressure in the future. Nevertheless, for the purpose of attracting more enterprises to settle in Xi'an ETDZ, the Company may receive government special-purpose bonds and interest subsidies from the local government to support the constructions.

Moreover, XKFH's supply chain business generated considerable amount of income but a relatively small gross profit margin. The Company conducts trading business mainly in non-ferrous metals, coal, steel, and chemical products. The Company adopts demand-on-purchase mode which means orders to upstream suppliers would be placed only when the sale contracts are signed with downstream customers. The concentration risks from upstream suppliers and downstream customers are high, with the top 5 suppliers and customers accounting for more than 60% of the total sales and total procurements, respectively.

Additionally, XKFH conducts equity investment and financial services, in order to promote the local industrial development. It has invested in several high-quality funds and equities across different sectors that focus on the key companies settled in Xi'an ETDZ. However, the return on XKFH's investments is subject to the macroeconomics, industry policy changes and capital market environment, which may exert higher uncertainties on future return. The Company provides comprehensive financial services to local small-medium enterprises including guarantee, factoring, and financial leasing. Although the operating scale is small, we will continue to pay attention to the operation and risk control of the Company's financial businesses, especially the contingent risk arising from its guarantee business.

Solid track record of receiving government support

XKFH and its subsidiaries have a solid track record of receiving support from the local government, as the Company's public-policy projects are strategically important to local development. The Company has received ongoing support from the local governments of Xi'an ETDZ, in terms of capital injections, special funds, interest subsidies, and operating subsidies. From 2020 to 2022, the Management Committee of Xi'an ETDZ injected capital of more than RMB791 million into the Company, which substantially enhanced the capital strength of the Company. Moreover, the local government provided continuous operating subsidies with the total amount of more than RMB331.3 million over the same period. In terms of interest subsidies, the Company received the amount of RMB297.0 million, RMB350.1 million, and RMB467.8 million in 2020, 2021, and 2022, respectively. Considering the Company's status as the most important LIIFC of Xi'an ETDZ, we expect XKFH will continue receiving support from the local government.

High debt leverage and increasing refinancing pressure

With the continuous financing of construction projects, XKFH's debt leverage remains high, and also shows an increasing refinancing pressure. As of 31 March 2023, the Company's total debt increased to RMB39.8 billion from RMB24.5 billion at end-2020; while its total capitalization ratio maintained a relatively high level of 69.5%, increasing from 66.1%. Moreover, the Company's liquidity profile weakened, as its short-term debt accounted for 40.9% of total debt as of 31 March 2023, significantly increasing from 22.5% at end-2020. At the same time, the Company reported cash and cash reserves of RMB7.6 billion, which can only cover around 47% of its short-term debt, indicating a high refinancing pressure. Therefore, we expect the Company to continue to rely on

external financing to meet its future capital needs, and its debt leverage will remain relatively high over the next 12 to 18 months.

Good access to funding and concentrated on bank loans

XKFH's large refinancing needs could be partially supported by its good refinancing ability. Most of the Company's increment debt consists of bank loan and it has maintained a good relationship with policy banks, large state banks and commercial banks. As of 31 March 2023, the Company has obtained total credit facilities of RMB119.3 billion, with an unutilized amount of RMB47.4 billion, reflecting sufficient liquidity buffer. Moreover, the Company and its subsidiary have participated in domestic debt capital market including corporate bonds and MTNs. They issued one tranche of corporate bonds and MTN in 2021 and 2022, respectively, raising the amount of RMB3.0 billion with coupon rates between 4.38% and 5.2%. It also has access to high-cost nonstandard financing channels such as trust and financial leasing to meet its funding needs. The Company had a certain proportion of these products which accounted for around 20% of total debt as of 31 March 2023.

We believe XKFH's market acceptance will be maintained whether it is the bond market or bank, taking into account the Company's important status as the largest entity in the local development of Xi'an ETDZ after successfully consolidating several LIIFCs in the region.

ESG Considerations

XKFH faces environmental risks because it has undertaken urban infrastructure construction and property development projects. Such risks could be moderated by conducting environmental studies and planning prior to the start of the projects, and close monitoring during the construction phase.

XKFH bears social risks as it is engaged in provision of diversified public utility services in Xi'an ETDZ. Demographic changes, public awareness and social priorities shape the Company's development targets and ultimately affect the local government's propensity to support the Company.

XKFH's governance considerations are also material as the Company is subject to oversight by the local government and has to meet several reporting requirements, reflecting its public-policy role and status as a government-owned entity. The Company maintains regular communication with local governments and regulatory authorities through its management team or representatives, ensuring compliance with the requirements and conditions for obtaining and maintaining the licenses, concessions, permits, or certificates.

Structural considerations

XKFH's senior unsecured debt rating is equal to its long-term credit rating. We believe that government support will flow through the Company given its essential role as the comprehensive urban developer and operator in Xi'an ETDZ, thereby mitigating any differences in an expected loss that could result from structural subordination.

Rating Methodology

The methodology used in this rating is the Rating Methodology for [China's Local Infrastructure Investment and Financing Companies \(July 2022\)](#).

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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