

Credit Opinion

31 October 2023

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

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Zibo Hi-Tech State-Owned Capital Investment Co., Ltd.

Surveillance credit rating report

CCXAP affirms Zibo Hi-Tech State-Owned Capital Investment Co., Ltd.'s long-term credit rating at BBB_g, with stable outlook.

Summary

The BBB_g long-term credit rating of Zibo Hi-Tech State-Owned Capital Investment Co., Ltd. ("ZBHT" or the "Company") reflects Zibo High-tech Zone Government's strong capacity to provide support and its extremely high willingness to provide support based on our assessment of the Company's characteristics.

Our assessment of Zibo High-tech Zone Government's capacity to support reflects its vital role as a national high-tech zone in Zibo City and Shandong Province, with strong economic growth, good fiscal metrics and debt profile.

The rating also reflects the local government's willingness to support, which is based on the Company's (1) dominant role in local infrastructure construction and land development; (2) providing utility services with high replacement cost; (3) good track record of receiving government payments; and (4) good access to diversified funding channels.

However, the Company's rating is constrained by (1) medium exposure to commercial activities with certain capital expenditure pressure; and (2) fast debt growth driven by large number of construction projects.

The stable outlook on ZBHT's rating reflects our expectation that the Zibo High-tech Zone Government's capacity to provide support will remain stable, and the Company will maintain its strategic importance in the development of Zibo High-tech Zone over the next 12 to 18 months.

Rating Drivers

- Dominant role in local infrastructure construction and land development
- Good track record of receiving government payments
- Medium exposure to commercial activities with certain capital expenditure pressure
- Good access to diversified funding channels
- Fast debt growth driven by large number of construction projects

Rating Sensitivities

What could upgrade the rating?

The rating could be upgraded if (1) Zibo High-tech Zone Government's capacity to provide support strengthens; and (2) the Company's characteristics change in a way that strengthens the local government's willingness to provide support, such as lowering exposure to risky commercial activities, and improving debt management.

What could downgrade the rating?

The rating could be downgraded if (1) Zibo High-tech Zone Government's capacity to provide support weakens; or (2) the Company's characteristics change in a way that weakens the local government's willingness to provide support, such as reduced strategic significance, decreased government payments, or increased exposure to commercial activities.

Key Indicators

	2020FY	2021FY	2022FY	2023H1
Total Asset (RMB billion)	33.6	47.5	61.4	68.5
Total Equity (RMB billion)	11.1	16.2	16.2	20.8
Total Revenue (RMB billion)	1.6	2.5	3.1	0.8
Total Debt/Total Capital (%)	55.2	55.1	62.1	58.5

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

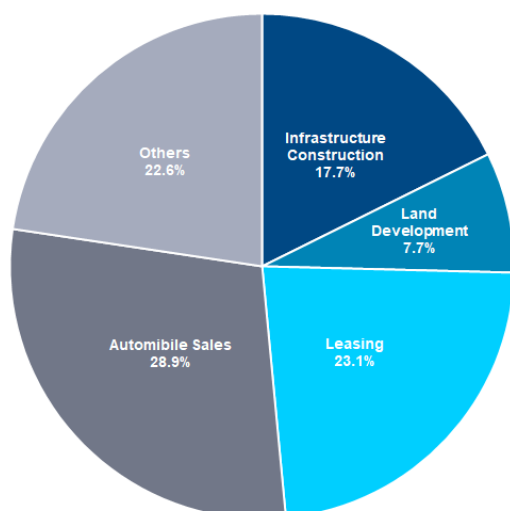
Source: Company information, CCXAP research

Corporate Profile

Founded in March 2019, ZBHT is the pivotal local infrastructure investment and financing company ("LIIFC") in Zibo Development Zone for New and High Technology Industries ("Zibo High-tech Zone"), with the second largest total assets in Zibo City. As of 30 June 2023, it was directly and wholly owned by the Finance Bureau of Zibo High-tech Zone, and the Administrative Committee of Zibo High-tech Industrial Development Zone remained its ultimate controller. In accordance with the economic development strategy and social development requirements of Zibo High-tech Zone, ZBHT is responsible for public infrastructure and welfare projects, including infrastructure construction, land development, and water supply. It also has commercial operations, including leasing, automobile sales, direct equity investments, and industrial investment fund businesses.

Exhibit 1. Shareholding chart as of 30 June 2023

Source: Company information, CCXAP research

Exhibit 2. Revenue structure in 2022

Source: Company information, CCXAP research

Rating Considerations**Government's Capacity to Provide Support**

We believe the local government of Zibo High-tech Zone has a strong capacity to provide support given its good economic fundamentals and fiscal strengths.

Shandong Province is the third largest province in terms of gross regional product ("GRP") in China over the past three years, with a solid industrial foundation in logistics, shipbuilding and marine technology, chemical, automotive and agri-food. Zibo City is located in the central part of Shandong Province, which is one of the core cities of Shandong Peninsula Urban Agglomeration and a regional central city in Shandong Province approved by the State Council. Zibo City recorded a GRP of RMB440.3 billion in 2022, ranking the 7th by GRP among 16 prefecture-level cities in Shandong Province over the past three years. Zibo City has strong relatively fiscal strength and a manageable debt profile. In 2022, its general budgetary revenue covered around 70% of its

general budgetary expenditure, and tax incomes accounted for nearly 65% of its general budgetary revenue. As of end-2022, Zibo City's government debt balance was RMB108.0 billion, accounting for 24.5% of GRP. In the first half of 2023, Zibo City's GRP was RMB229.5 billion, a year-over-year ("YoY") increase of 5.3%.

Exhibit 3. Key Economic and Fiscal Indicators of Zibo City

	2020FY	2021FY	2022FY
GRP (RMB billion)	367.4	420.1	440.3
GRP Growth (%)	2.5	9.4	4.7
General Budgetary Revenue (RMB billion)	32.2	36.9	37.6
General Budgetary Expenditure (RMB billion)	52.3	52.3	52.6
Local Government Debt (RMB billion)	77.5	94.6	108.0

Source: Statistics Bureau of Zibo City, CCXAP research

Zibo High-tech Zone is a national-level high-tech zone with the approval of the State Council of China in 1992. It is a national new materials industrialization base named by the Ministry of Science and Technology of China. It is also a National Innovation Demonstration Zone ("国家自主创新示范区") and Pilot Zone of New and Old Kinetic Energy Conversion ("新旧动能转换试验区") in Shandong Province, as well as a provincial economic development zone established with the approval of Shandong Provincial Government. Zibo High-tech Zone has developed some core industries, including new energy manufacturing, intelligent microsystems, big health, new materials and financial technology industries. It has demonstrated stable economic growth in recent years. In 2022, the GRP of Zibo High-tech Zone increased by 12.1% YoY to RMB37.8 billion, as compared to that of 11.9% in 2021. In addition, Zibo High-tech Zone has a good financial self-sufficiency, with fiscal balance ratios (general budgetary revenue/general budgetary expenditure) above 100% over the past three years. It also has a moderate debt profile, with a government debt/GRP ratio of 30.2% as of 31 December 2022. In the first half of 2023, the GRP of Zibo High-tech Zone was RMB21.9 billion, a YoY increase of 6.1%.

Exhibit 4. Key Economic and Fiscal Indicators of the Zibo High-tech Zone

	2020FY	2021FY	2022FY
GRP (RMB billion)	28.5	33.7	37.8
GRP Growth (%)	8.2	11.9	12.1
General Budgetary Revenue (RMB billion)	3.9	4.8	4.8
General Budgetary Expenditure (RMB billion)	3.8	4.0	4.1
Local Government Debt (RMB billion)	6.8	8.9	11.4

Source: Management Committee of Zibo High-tech Zone, CCXAP research

Government's Willingness to Provide Support

Dominant role in local infrastructure construction and land development

ZBHT is the first-level holding company under the Zibo High-tech Zone Government and the sole LIIFC in Zibo High-tech Zone, which has a clear strategic role in regional development. The Company is commissioned to carry out various key infrastructure construction, land development projects and water supply business that are crucial to local economic development and benefit the general public and local employment.

The Company and its subsidiaries are engaged in the infrastructure construction business through the entrusted construction model and the government purchase model. Under the entrusted construction model, the Company signs an entrusted construction agreement with the government before each project is developed, and transfers

the project ownership to the government or related parties after the project is completed. The government will pay the total cost plus a certain markup after examining the projects. Under the government purchase model, the Company manages infrastructure projects assigned by the local government according to the agreements and receives construction costs and service fees annually. Projects completed by ZBHT included schools, elderly rehabilitation centers, new countryside construction projects, and urbanization construction projects. As of 30 June 2023, the Company had 5 key construction projects under construction, including shantytown renovation and river ecological management, with a total investment of RMB5.5 billion and an uninvested amount of RMB1.6 billion. Large-scale projects in the pipelines will ensure the sustainability of the business.

Additionally, the Company launched the land development business in 2019 and adopted the entrusted construction model. The Company is entrusted to develop and consolidate the land parcels of 82 square kilometers within the four boundaries of Jiqing Highway, Yellow River Avenue, Lushan Avenue and Binlai Highway in Zibo High-tech Zone, with an estimated total investment of RMB5.0 billion. The Company is expected to receive project repayments based on the actual cost plus a markup in return, generally 15%. As of 30 June 2023, ZBHT's land consolidation projects had an estimated outstanding investment of RMB3.7 billion, exerting certain capital expenditure pressure on the Company.

ZBHT also provides water supply service to residents and industrial enterprises in Zibo High-tech Zone at prices guided by local government. The Company has a relatively long concession for water supply business with over 20 years, which generating stable income to the Company, demonstrating strong sustainability. As of end-2022, the Company had water pipelines with a total length of 170 kilometers, providing water supply to a population of around 56,000 within a coverage area of 35 square kilometers. We believe that the replacement cost for the Company's role is high as these public services are essential for the region.

Medium exposure to commercial business activities with certain capital expenditure pressure

ZBHT's major commercial businesses include property leasing, automobile sales, direct equity investments, and industrial investment fund businesses, with relatively high capital expenditure pressure. Most of these commercial activities are policy-driven which are related to public policy businesses. ZBHT's commercial businesses are responsible for attracting high-tech companies to settle in Zibo High-tech Zone, which helps support regional economic development. Although the commercial assets account for more than 30% of total assets by the end of June 2023, we estimate the Company's risk exposure to commercial business is moderate.

ZBHT has high-quality leasing assets which provides additional recurring income. The Company is responsible for attracting investment in Zibo High-tech Zone and providing preferential rents for settled enterprises. Its projects mainly focus on industrial parks, office buildings, and factories, with a total leasable area of around 2.0 million square meters, most of which have been lease out. With the completion of the newly constructed leasing assets in 2022, the leasing income in 2022 increased to RMB727.3 million from RMB509.1 million in 2021. As of 31 March 2023, the Company had numbers of leasing projects under construction, with a total investment of RMB26.4 billion and an outstanding investment of RMB16.7 billion. The construction costs of some leasing properties were financed through local government special bonds, which could partially ease the Company's capital expenditure pressure.

ZBHT also conducts direct equity investment and fund investment business. The Company had participated in the establishment of industrial investment funds and invested in several industries such as new materials, medicine, electronic information, and intelligent equipment manufacturing. As of end-2022, the value of the Company's fund investment and direct equity investment had reached RMB3.6 billion and RMB2.0 billion, respectively. As most of the direct investment targets are private startup enterprises, the return on investment

is subject to great uncertainty. Some of them are listed companies, such as Polestar Automotive Holding Limited, and the investment income would be recorded in the next few years. Furthermore, the Company's direct investment also makes it bear certain risk exposure to local private-owned enterprises, which have higher operation risks during market downturn.

ZBHT's automobile sales business started to generate income in 2022, mainly including new energy vehicles. The Company has a vehicle manufacturing factory with a designed production capacity of 100,000 pure electric passenger vehicles. The Company mainly adopts procurement-on-demand model, and orders to upstream suppliers and production plans would be made based on the actual sales. The revenue of automobile sales business recorded RMB909.0 million, accounting for 28.9% of the Company's total income in 2022. However, the Company recorded a negative gross profit margin at the early stage of this business.

Good track record of receiving government payments

ZBHT has a proven track record of receiving support from the local government in terms of capital injections, asset injections, and subsidies. From 2022 to 2023H1, the company received capital injection in terms of cash of RMB948.2 million from the Finance Bureau of Zibo High-tech Zone. Apart from that, the local government also transferred equity shares of some state-owned enterprises and franchise rights to the Company in 2022, with a total value of RMB157.5 million. By the end of June 2023, the Company's capital reserve has increased to RMB15.3 billion from RMB7.6 billion as of end-2020.

In addition, ZBHT also has a good track record of receiving government payments. In 2022, ZBHT continuous to receive government subsidies with a total amount of around RMB1.2 billion, including interest subsidy and operating subsidy, which are good support for its future investments and constructions. As of 30 June 2023, ZBHT has received total project repayments of RMB8.2 billion from the local government for its infrastructure construction and land consolidation projects. We expect that, as the largest local state-owned enterprise in Zibo High-tech Zone, the Company plays an irreplaceable role in the development and operation of the region, and the local government has an extremely high willingness to provide support to the Company.

Fast debt growth driven by large number of construction projects

Due to the continuous investment in infrastructure construction projects, ZBHT's total debt has been growing rapidly over the past three years. As of 30 June 2023, the Company's total debt increased to RMB29.3 billion from RMB13.6 billion as of end-2020, while the total capitalization ratio rose slightly from 55.2% to 58.5%. The Company's liquidity profile is moderate. As of 30 June 2023, the Company's short-term debt amounted to RMB11.3 billion, accounting for 38.7% of the total debt. Moreover, its cash to short-term debt ratio was 0.2x, indicating certain short-term debt repayment pressure. Given the Company's large capital expenditure pressure for its investment and construction projects under construction, we expect the Company will maintain a relatively high level of debt for the next 12-18 months.

Good access to diversified funding channels

ZBHT had shown good access to various sources of funding, including bank loans and onshore and offshore bond financing. The Company maintains good long-term relationships with several banks. As of 30 June 2023, the Company had total credit facilities of RMB25.4 billion, with an unutilized portion of RMB10.1 billion. The credit facilities were provided by diversified domestic banks, including national joint-stock commercial banks, large state-owned commercial banks, and policy banks, such as Agricultural Development Bank of China.

The Company also has a good track record for fund-raising activities in capital market. For example, in 2022, the Company raised around RMB1.8 billion from onshore bonds, It also has an access to offshore bond market. From January to September 2023, ZBHT issued 4 tranches of offshore bonds, raising USD157.2 million. As of 30 June 2023, the Company's exposure to non-standard financing is generally controllable, accounting for around 20% of the total debt. Besides, the proportion of non-standard borrowings is expected to decrease given the Company's diversified financing channels. Considering the Company's important status as the sole platform conducting public policy projects in Zibo High-tech Zone, we expect ZBHT to maintain access to domestic bank loans and capital markets.

ESG Considerations

ZBHT assumes environmental risks through its infrastructure and land development projects. Such risks could be moderated through environmental studies and detailed planning prior to the start of the projects and close supervision during construction.

In terms of social concerns, the Company plays a crucial role in the social welfare of the residents in Zibo High-tech Zone by conducting infrastructure construction projects. In addition, as the largest state-owned entity in Zibo High-tech Zone, the Company has taken a number of measures to ensure the provision of utility and the daily needs of the residents. It also provided rent relief to local enterprises during the pandemic control period.

In terms of corporate governance, the Company has established an effective corporate governance structure consisting of investors, party committee, the board of directors, board of supervisors, general manager, and the management team, and has formulated the rules and procedures for meetings of the party committee, the board of directors, the board of supervisors and the general manager's office. In addition, ZBHT is subject to oversight and reporting requirements of the Zibo High-tech Zone Government, which has full control and supervision over the Company's operations.

Structural Consideration

ZBHT's senior unsecured debt rating is equivalent to its long-term credit rating. We believe that government support will flow through the Company given its strategic importance in the development of Zibo High-tech Zone, 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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