

Credit Opinion

31 May 2024

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

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Changde Economic Construction Investment Group Co., Ltd.

Initial credit rating report

CCXAP assigns first-time long-term credit rating of BBB_g+

to Changde Economic Construction Investment Group Co., Ltd., with stable outlook

Summary

The BBB_g+

Our assessment of Changde Municipal Government's capacity to provide support reflects Changde City's economic and fiscal importance in Hunan Province, with ongoing economic growth.

The rating also reflects the local government's willingness to provide support, which is based on the Company's (1) important position in urban development and construction of Changde City; (2) key role in public services essential to the social welfare and economic development of Changde City; and (3) good track of receiving government support.

However, the rating is constrained by the Company's (1) medium exposure to commercial activities; (2) fast debt growth due to large capital expenditure pressure; and (3) moderate exposure to contingent liabilities.

The stable outlook on CECI's rating reflects our expectation that the local government's capacity to provide support will remain stable, and the Company will maintain its status as important urban development and construction entity in Changde.

Rating Drivers

- Important position in urban development and construction of Changde City
- Key role in public services essential to social welfare and economic development
- Medium exposure to commercial activities
- Good track of receiving government support
- Fast debt growth due to large capital expenditure pressure
- Moderate exposure to contingent liabilities

Rating Sensitivities

What could upgrade the rating?

The rating could be upgraded if (1) the local 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 strengthened regional significance or reduction in the exposure to commercial activities.

What could downgrade the rating?

The rating could be downgraded if (1) the local 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 or weakened access to funding.

Key Indicators

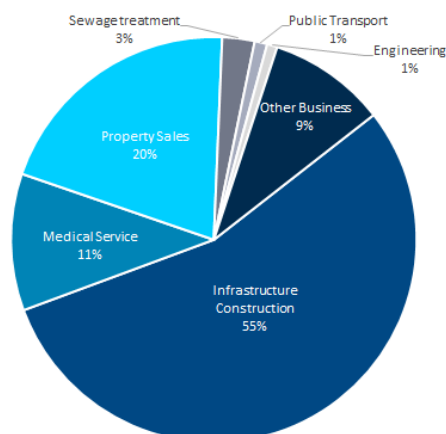
	2021FY	2022FY	2023FY
Total Asset (RMB billion)	96.5	104.3	110.1
Total Equity (RMB billion)	33.7	38.6	42.3
Total Revenue (RMB billion)	6.6	6.1	4.7
Total Debt/Total Capital (%)	59.4	57.2	54.7

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

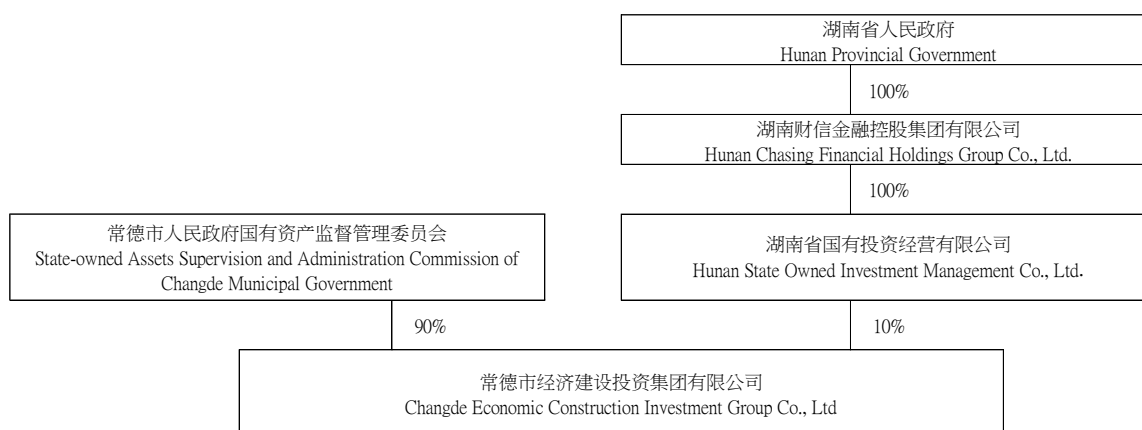
Source: Company data, CCXAP research

Corporate Profile

Established in 1992, CECI is one of the key local infrastructure investment and financing companies ("LIIFC") in Changde City and has played a key role in the construction and development of major infrastructure in Changde. The Company is mainly engaged in infrastructure construction, sewage treatment and public transportation in Changde City. It is also participated in commercial activities such as real estate development and medical services. As of 31 December 2023, the Company was 90% owned and ultimately controlled by the State-owned Assets Supervision and Administration Commission of Changde Municipal Government ("Changde SASAC"). Hunan State Owned Investment Management Co., Ltd holds the remaining 10% of the Company's shares.

Exhibit 1. Revenue structure in 2023

Source: Company information, CCXAP research

Exhibit 2. Shareholding chart as of 31 December 2023

Source: Company information, CCXAP research

Rating Considerations

Government's Capacity to Provide Support

We believe that the Changde Municipal Government has very strong capacity to provide support, given its economic and fiscal importance in Hunan Province, with ongoing economic growth.

Located in the central part of China, Hunan Province is one of the important cradles of Chinese civilization and it is also an important grain production base. In 2023, the gross regional product ("GRP") of Hunan Province was RMB5.0 trillion, ranking 10th among all provinces in China. Benefited from economic recovery and industrial development, its general public budget revenue decreased to RMB336.1 billion in 2023 from RMB310.2 billion in 2022, with tax revenue accounting for 65.7% of its general public budget revenue.

Located in the north of Hunan Province, Changde City is at the junction of the Pan-Pearl River Delta and Pan-Yangtze River Delta economic development regions. Changde City is an important national agricultural production base. It has formed its pillar industries including food, textile, electromechanical, chemical and

building materials. Benefiting from its geographical and industries advantages, Changde City's GRP increased from RMB405.4 billion in 2021 to RMB438.6 billion in 2023, ranking 3rd by GRP among 14 prefecture-level divisions in Hunan Province. Changde Municipal Government's general budgetary revenue remained at RMB20.3 billion in 2023 compared with 2021, with tax income accounting for 53.0% of its fiscal revenue in 2023. However, its fiscal balance is relatively weak, with a general budgetary revenue/general budgetary expenditure ratio of 33.4% on average over the past three years. At the end of 2023, Changde's local government debt balance was RMB110.5 billion, accounting for 25.2% of GRP.

Exhibit 3. Key Economic and Fiscal Indicators of Changde City

	2021FY	2022FY	2023FY
GRP (RMB billion)	405.4	427.5	438.6
GRP Growth (%)	7.7	4.5	3.6
General Budgetary Revenue (RMB billion)	20.3	20.8	20.3
General Budgetary Expenditure (RMB billion)	59.7	63.0	61.3
Local Government Debt (RMB billion)	80.1	92.3	110.5

Source: Statistics Bureau of Changde City, CCXAP research

Government's Willingness to Provide Support

Important position in urban development and construction of Changde City

There are four key LIIFCs in Changde City, each responsible for the development of different area in Changde City without overlapping. The Company is an important LIIFC with the second largest assets size in Changde City, and mainly responsible for the infrastructure construction projects in the eastern part of Wuling Avenue in Changde City. The Company has participated in series of public policy business including infrastructure construction, sewage treatment, public transportation services, medical service, shantytown renovation and resettlement housing. Considering that CECl has strong regional importance in Changde City, we believe that the Company will remain its role as an important urban development and construction entity in Changde City and will not be easily replaced by other state-owned enterprises in the foreseeable future.

CECl undertakes infrastructure construction projects under agency construction model. The Company conducts infrastructure construction projects by signing agency construction agreements with the local government, which will settle with the Company based on the project investment amount plus 18% markup upon project completion. As of 31 December 2023, the Company had completed 115 infrastructure construction projects, with total investment amount of RMB19.0 billion. Besides, CECl had 7 infrastructure projects under construction, with a total planned investment of RMB1.6 billion and an uninvested amount of RMB864.4 million. However, the Company has no infrastructure construction projects under planning.

Authorized by Changde Municipal Government, CECl has been conducting shantytown renovation projects in Changde City through its subsidiaries. After finishing the house demolition and local government auctioning, the Company is responsible for the construction and sales after obtaining the land use-right. The remaining houses will be sold in the market after satisfying the needs of resettlement residents. The Company finances shantytown renovation projects in advance, and achieves fiscal balance through government subsidies or sale of remaining houses. From 2021 to 2023, CECl received government subsidies of RMB153.6 million for shantytown renovation projects. As of 31 December 2023, the Company had completed 13 shantytown renovation projects, with total recognized payment of around RMB4.0 billion. Besides, CECl had 6 shantytown renovation projects under construction or planning, with a total planned investment of RMB3.7 billion and an uninvested amount of RMB1.5 billion, indicating certain pressure on the Company's capital expenditure.

CECI is also a primary developer of resettlement housing in Changde City. The local government will coordinate resettlement housing allocation and sell them under at market prices. The Finance Bureau of Changde City will receive the revenue and then pay back to the Company. As of 31 December 2023, the Company had completed 34 resettlement housing projects, with repayment amount of RMB2.8 billion. Besides, CECI had no resettlement housing projects under construction or planning.

CECI provides sewage treatment services within Changde City. The Company operates the only sewage treatment plant in Changde and is committed to improving water quality and sewage treatment in Changde. Besides, the Company had also constructed various sewage pumping stations and sewage treatment plants in Changde. In addition, CECI introduced a new technology to control ecological pollution and became a model for “Sponge City”, an urban sewage management concept nationwide which enables the sewage system to function with flexibility in adapting to changing ecological environment. From 2022 to 2023, the Company recorded revenue of RMB240.0 million in this area. As the Company has strong competence and relatively monopoly status in Changde City, the Company is expected to receive continuous government support and maintain its key role in sewage treatment services.

Besides, the Company also provides public transportation service in Changde City. CECI conducts its public transportation services business primarily through its wholly-owned subsidiary, Changde Public Traffic Co., Ltd, which is a major public bus operator in Changde and mainly responsible for providing passenger transportation services in Changde and nearby suburban areas. It generates revenue from ticket selling and advertisement services alongside public transportation. As of 31 December 2023, CECI operated 53 bus routes and had daily passenger flow of 163,861. Since CECI has monopoly status in Changde City, the Company is expected to maintain its key role in public transportation services.

Medium exposure to commercial activities

In addition to public activities, CECI is also engaged in commercial businesses, including sale of commercial properties and medical products. We consider the Company’s exposure to commercial businesses to be medium, accounting for around 25% of its total assets. However, commercial risk is moderate since property sales business is greatly affected by the changes in regional property market. Besides, medical products business is strictly regulated by the government and may fluctuate due to policy changes.

CECI conducts property sales business through its subsidiary. This business provides supplementary income to the Company. In 2023, the Company generated revenue of around RMB951.6 million, with a gross profit margin rate of around 5.5%. As of 31 December 2023, there were no commercial housing projects under construction or planning. However, this business exposes to high business risk due to its high reliance on market prospects, especially under the gloomy outlook of the property market in recent years.

In addition, CECI has several self-operating projects, mainly including citizen home project and industrial park. The Company will achieve fiscal balance through the income from rentals, management fees and parking fees in the future, with an estimated payback period of 5-7 years. However, the Company faces fiscal balance problems because of the long payback period for these self-operating projects.

The healthcare sector generated revenue of RMB663.6 million and RMB509.5 million in 2022 and 2023. CECI delivers high-quality healthcare services through the operation of Xiangya Changde Hospital, a Grade III comprehensive hospital in Changde which is invested and constructed by CECI. CECI previously operated the Second People’s Hospital of Changde, a Grade III comprehensive hospital, which was transferred out of the Company in January 2022. With its brand advantage, Xiangya Changde Hospital has good future development

potential, and healthcare services sector may become an important revenue growth driver for the Company in the future. Due to the high construction costs and early operation period of Xiangya Changde Hospital, its gross profits had recorded loss in both 2022 and 2023. Considering the public importance of healthcare services, the local government has provided subsidies of totally RMB1 billion to the Company in the past three years. Nevertheless, as these hospitals are non-profit medical institutions, the government subsidies are not enough to cover its cumulated losses.

Apart from operating Xiangya Changde Hospital, CECI also conducts medical products sales, through its wholly-owned subsidiary, Changde Jingkang Pharmaceutical Co., Ltd (“Changde Jingkang”), which is in the first batch of enterprises that has been granted the new Goods Supply Practice qualification. Changde Jingkang primarily deals in medical products and medical instruments, with sales area concentrating in Changde City and nearby cities. This business is relatively stable as major customers of Changde Jingkang are Grade III hospitals in Changde City. Settlement period between Changde Jingkang and its customers is about 6 months. However, revenue of Changde Jingkang declined in 2023 due to the centralized procurement policy of medicine.

Apart from property sales and medical services, the Company also has some other commercial businesses. All of those businesses have relatively small size and provide supplementary revenue to the Company.

Good track of receiving government support

CECI has regularly received support from the local government in the form of special fund, government purchase, operating subsidy and capital injection. Undertaking key projects in the region, the Company has received ongoing special fund from the government of totally RMB6.2 billion as of end-2023. Besides, the Company has also received government payment for urban infrastructure construction projects of RMB8.7 billion. In 2011, Changde SASAC has injected Zhantian Lake sewage treatment plant and parts of urban road drainage network with an evaluation value totaling RMB582 million to the Company. In 2022, it also has transferred the franchise rights of the river channel to the Company, increasing the capital reserve of RMB4.3 billion. Furthermore, the Company also receives operating subsidy from the local government, totaling RMB2.5 billion from 2021 to 2023. Given its status as important urban development and construction entity in Changde City, we believe that the local government will continue to provide support to the Company.

Fast debt growth due to large capital expenditure pressure

CECI has a relatively fast debt growth over the past three years. The Company’s total debt had increased from RMB48.0 billion at end-2021 to RMB51.2 billion at end-2023, with total capitalization ratio at relatively high level of 54.7%. The increase in debt is mainly attributable to the ongoing external financing for infrastructure construction projects. In addition, as of 31 December 2023, the Company’s short-term debt accounted for about 34.6% of total debt and its cash to short-term debt ratio was 0.2x, indicating relatively high short-term debt repayment pressure. Given its large capital expenditure pressure, we expect the Company’s debt burden will continue to grow in the next 12 to 18 months.

Moderate asset liquidity

CECI’s asset liquidity is moderate, which may undermine its financial flexibility. The Company’s assets mainly consist of inventories, receivables and contract assets, accounting for around 67% of its total assets as of 31 December 2023, all with relatively low liquidity. The inventories and contract assets are development costs from property development and infrastructure construction projects, and the receivables mainly consist of uncollected payments from the local government and other state-owned enterprises. However, the Company has certain

amount of cash reserves to support its daily operations and debt repayment. As of 31 December 2023, its cash reserves amounted to RMB4.1 billion, accounting for about 4% of total asset. In addition, the investment properties are mainly properties for leasing, while the intangible assets are mainly franchise rights of public transportation, which can provide certain cash flow and supplementary income to the Company.

Good access to diversified funding

CECI has good access to diversified funding from both banks and capital markets. The Company has an approved line of credit from both commercial banks and policy banks, such as China CITIC Bank and China Development Bank. As of 31 December 2023, it had obtained total credit facilities of RMB53.5 billion, with available credit facilities of RMB21.2 billion. The Company and its subsidiaries have high reliance on capital markets with moderate refinancing ability, accounting for 63.1% among all the funding channels. CECI has issued multiple bond products, such as PPNs, MTNs, SCPs and private corporate bonds on both onshore and offshore capital markets, raising about RMB34.8 billion, USD428.0 million and EUR263.0 million from 2021 to 2023. CECI's refinancing is largely affected by the changes in bond issuance policies and capital market situations, given its high reliance on bond financing. In addition, CECI has moderate exposure to non-standard financing, which accounted for 12.1% of its total debts at end-2023.

Moderate exposure to contingent liabilities

CECI's external guarantee exposure is moderate. As of 31 December 2023, its external guarantee amount was RMB8.7 billion, accounting for 20.5% of its total equity. Most external guarantees of the Company are provided to state-owned enterprises in Changde City. In case a credit event occurs, the Company may face certain contingent liability risks and cross default risks, which could negatively impact its credit quality.

ESG Considerations

CECI faces environmental risks because it has undertaken infrastructure development and construction 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.

CECI bears social risks as it implements public policy initiatives by undertaking infrastructure development and construction projects in Changde City. 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.

CECI's governance considerations are also material as the Company is subject to oversight by the Changde Municipal Government and has to meet several reporting requirements, reflecting its public-policy role and status as a government-owned entity.

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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