

Credit Opinion

19 June 2024

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

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Jingdezhen Hesheng Industrial Investment Development Co., Ltd.

Initial credit rating report

CCXAP assigns first-time long-term credit rating of BBB_g- to Jingdezhen Hesheng Industrial Investment Development Co., Ltd., with stable outlook.

Summary

The BBB_g- long-term credit rating of Jingdezhen Hesheng Industrial Investment Development Co., Ltd. (“Jingdezhen Hesheng”) is underpinned by the Company’s (1) investment portfolio in line with Jingdezhen City’s development strategy; and (2) diversified sources of revenue.

However, the rating is constrained by the Company’s (1) weak asset liquidity and weak profitability from investments; (2) increasing debt burden with large debt maturities; and (3) moderate access to funding.

The rating also reflects a moderate likelihood of government support from the Jingdezhen Municipal Government and its parent company when needed, which is based on the Company’s (1) ultimate control by the Jingdezhen Municipal Government; (2) significance in promoting the development of strategic emerging industries in Jingdezhen City; and (3) solid track record of receiving support from the local government and its parent company.

The stable outlook on Jingdezhen Hesheng’s rating reflects our expectation that the Company will continue to receive solid support from the Jingdezhen Municipal Government and its parent company. We also expect the Company to maintain a stable and prudent investment strategy over the next 12 to 18 months.

Rating Drivers

- Investment portfolio in line with Jingdezhen City's development strategy
- Diversified sources of revenue
- Weak asset liquidity and weak profitability from investments
- Increasing debt burden with large debt maturities
- Moderate access to funding
- Moderate likelihood of support from the Jingdezhen Municipal Government

Rating Sensitivities

What could upgrade the rating?

The rating could be upgraded if (1) the likelihood of support from the Jingdezhen Municipal Government and its parent company increases; (2) the quality of the Company's investment portfolio materially improves, such as having a higher level of asset liquidity and generating better recurring cash flow from investees; or (3) the Company's credit metrics improve, for example, a lower debt-to-investment income ratio and a higher cash-to-short-term debt ratio.

What could downgrade the rating?

The rating could be downgraded if (1) the likelihood of support from the Jingdezhen Municipal Government and its parent company decreases; (2) the performance of the Company's investment portfolio deteriorates; or (3) the Company shows weakened access to funding and eroded liquidity profile.

Key Indicators

Consolidated Level	2021FY	2022FY	2023FY
Total Assets (RMB million)	27,324.1	32,350.3	35,535.4
Total Equity (RMB million)	15,638.1	18,358.2	17,362.8
Total Revenue (RMB million)	1,120.0	2,388.9	1,075.8
Net Profits (RMB million)	114.8	102.3	42.3
Return on Equity (%)	0.9	0.6	0.2
Holding Company Level (HoldCo)	2021FY	2022FY	2023FY
Total Assets (RMB million)	24,061.0	28,042.2	31,067.4
Total Equity (RMB million)	14,781.0	15,888.1	16,004.5
Return on Equity (%)	0.4	0.8	0.6
Debt/Investment Income (x)	105,937.3	110,250.9	40,094.4
Cash/Short-term Debt (x)	0.5	0.2	0.2

All ratios and figures are calculated using CCXAP's adjustments.
Source: Company information, CCXAP research

Corporate Profile

Established in 2009, formerly known as Jingdezhen Hesheng Optoelectronics Industrial Investment Development Co., Ltd, Jingdezhen Hesheng is positioned as an important industrial investment platform in Jingdezhen City, focusing on the investment in emerging industries such as aviation, new energy, and new materials. In addition, the Company is also involved in property leasing, real estate, and trading businesses. As of 31 December 2023, Jingdezhen Hesheng was 80% owned by Jingdezhen Investment Co., Ltd., (“Jingdezhen Investment”), which was Jingdezhen City’s main industrial investment platform and wholly owned by Jingdezhen State-owned Assets Operation and Investment Holding Group Co., Ltd. (“JSAH”), while Management Committee of Jingdezhen High-tech Industrial Development Zone (“Jingdezhen HIDZ”) held the remaining 20%. Its ultimate controlling shareholder is Jingdezhen State-owned Assets Supervision and Administration Commission (“Jingdezhen SASAC”).

Exhibit 1. Revenue structure in 2023

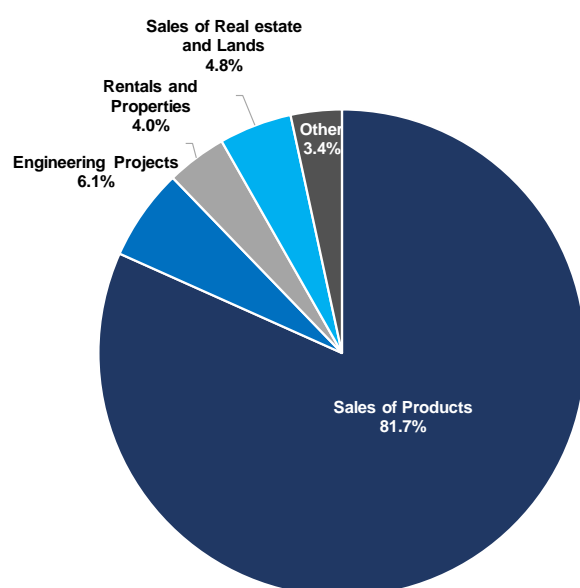
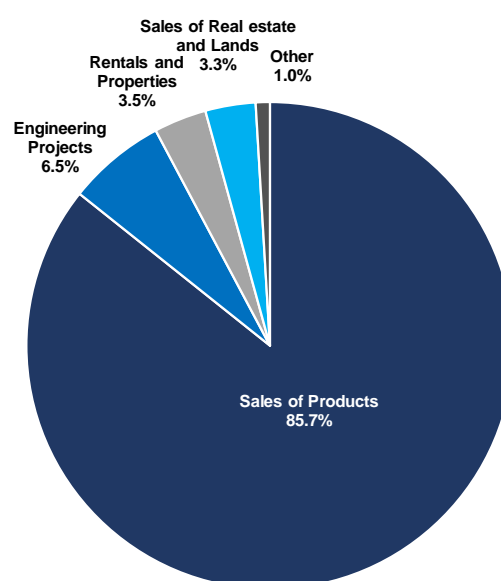
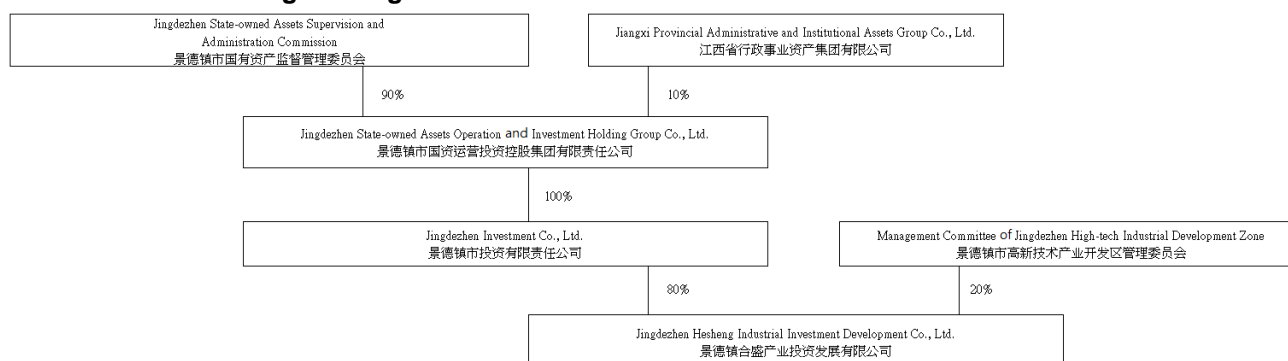


Exhibit 2. Gross profit structure in 2023



Source: Company information, CCXAP research

Exhibit 3. Shareholding and organization chart as of 31 December 2023



Source: Company information, CCXAP research

Rating Considerations

Investment portfolio in line with Jingdezhen City's development strategy, but with weak asset liquidity

In December 2023, JSAH, the largest investment and financing company in Jingdezhen City, swapped its equity interests of four subsidiaries with the Company's equity interests of two subsidiaries. After the equity swap, the Company will no longer undertake agency construction business. As an important industrial investment platform under the management of JSAH, Jingdezhen Hesheng is of great significance in promoting the development of strategic emerging industries in Jingdezhen City. The Company's investment portfolio is aligned with the government policies and economic development, mainly investing in emerging industries such as aviation, new energy, and new materials. However, the proportion of listed companies is relatively low and the proportion of single investment is relatively high, indicating weak asset liquidity and relatively high asset concentration.

The holding company is engaged in equity investment through direct holding of its subsidiaries' equity, which is the main component of its investment portfolio. Among them, Jingdezhen Fengshushan Forestry Limited ("Fengshushan Forestry") is the largest investment, accounting for 48% of the investment portfolio. It is mainly responsible for the management of forest assets in Fengshushan Mountain with book value of RMB6.5 billion. However, Fengshushan Forestry has low revenue and profitability. The holding company also directly holds 22.13% of the equity of a listed company Guangdong Zhengye Technology Co., Ltd. ("Zhengye Technology", stock code: 300410.SZ). With its optical testing and automation control technology, Zhengye Technology focuses on high-end industrial testing, including the testing of lithium battery, PCB, flat panel display as well as semi-conductor. As of 31 December 2023, the holding company direct held 22.13% equity interests of Zhengye Technology, with market value of RMB714 million, accounting for 4.6% of the investment portfolio. In addition, the Company has pledged about 48.9% of its holdings of Zhengye Technology, which undermines its financing flexibility.

The holding company also invests in key industries in Jingdezhen City through industrial funds, mainly involving emerging industries such as aviation, new energy and new materials. As of 31 December 2023, it had invested in 8 industrial funds, with accumulated subscriptions of RMB932 million and paid-in investments of RMB212 million. At present, its investment income mainly includes dividends. However, most of the investment projects are still in the early stages, with small dividend scale. As of 31 December 2023, the book value of the funds held by the holding company was RMB191 million, accounting for small proportion of investment portfolio.

Diversified sources of revenue

The Company has diversified income from different business segments, including precision machinery inspection equipment and materials, property leasing, real estate, and trading. We believe that the diversified business portfolio can diversify its business risks, but some of the businesses have exerted certain capital expenditure pressure to the Company.

The precision machinery inspection equipment and materials business operated by Zhengye Technology is the largest income source of the Company. In 2023, the revenue from this business accounted for 69.9% of total revenue. However, the revenue of Zhengye Technology has decreased significantly since 2022 as the orders declined, which has also caused certain goodwill impairments. The operating and goodwill impairment risks may undermine the revenue and profits of Zhengye Technology. In addition, Zhengye Technology has invested in a construction project of 5GW photovoltaic modules and 8GW heterojunction photovoltaic cell production base, with a total investment of RMB5 billion, indicating certain investment risks and capital expenditure

pressure.

The Company also owns leasable properties including industrial and commercial buildings, providing supplementary income to the Company. In 2023, the Company's property leasing business achieved income of RMB43.1 million, with a gross profit margin of 18.3%. As of 31 December 2023, the Company had leasable factory buildings of 947 thousand square meters with moderate occupancy rate of around 48%. At present, the Company mainly relies on self-owned funds as well as external financing to conduct large amount of self-operated projects, which will be sold or leased after completion of construction. As of 31 December 2023, the Company had 11 projects under construction with total estimated investment of RMB7.4 billion and uninvested amount of around RMB3.3 billion, as well as 5 projects under planning with total estimated investment of RMB4.5 billion, exerting high capital expenditure pressure to the Company. Nonetheless, some of the projects are supported by the government special bonds, partly alleviating its investment pressure.

The Company has participated in real estate development in Jingdezhen HIDZ, mainly involving construction and development of resettlement housing. The Company primarily carries out the construction projects under agent construction model. Upon completion of the project, the Company will sell the resettlement housing to relocated households in accordance with the government guided prices. At present, it has one completed resettlement housing project, with moderate sell-through rate of 47.2%. As of 31 December 2023, the Company had only one project under construction, with total estimated investment of RMB866 million and uninvested amount of RMB190 million. However, the project under construction is expected to be completed in 2024 and there is no project under planning, indicating uncertain sustainability for this business.

In addition, the Company has participated in trading business through its subsidiary, with trading products mainly including steels, and concrete, which are sold to large-scale construction state-owned enterprises or industrial park enterprises, earning profits from the price difference of the goods bought and sold. In addition, this business is subject to concentration risks as the Company has high reliance on its top 5 customers and suppliers. In 2023, the sale to the top five customers accounted for 91.3% of the total sale and the procurement to the top five suppliers accounted for 78.4% of the total procurement. This business provides supplementary income to the Company, with revenue accounting for around 10% of total revenue in 2023.

Weak profitability from investments

The Company's profitability is weak, mainly due to its low investment income, which weaken its ability to repay debts through its internal financial resources. In 2023, its investment income at holding company level amounted to as low as RMB223.9 thousand, insufficient to cover annual interest expenses of over RMB500 million. As a result, the Company's interest payment and profit rely heavily on government subsidies. In 2023, the Company reported a net income of RMB97.0 million at holding company level, with low ROE of 0.6%, indicating weak profitability.

Increasing debt burden with large debt maturities

Owing to the increasing capital demand for investment, Jingdezhen Hesheng's debt burden has increased in the past years. The Company's adjusted total debt increased from RMB10.1 billion at end-2021 to RMB15.1 billion at end-2023 at consolidated level, and increased from RMB7.8 billion at end-2021 to RMB9.0 billion at end-2023 at holding company level. The Company relies on external funds to refinance its debt as most of the debts are from the holding company with very low investment income. We expect the Company's debt burden will continue to increase, given its large capital expenditure needs for its extensive construction projects and industrial investment. In addition, the Company has relatively high short-term debt repayment pressure. As of

31 December 2023, the short-term debt amounted to around RMB3.7 billion at holding company level, representing 35.9% of its total debt, and the cash to short-term debt ratio was 0.2x at holding company level.

Moderate access to funding

The Company has access to debt capital markets. From January 2021 to March 2024, the Company raised RMB1.7 billion through the onshore debt market. Additionally, the Company also had raised RMB536.3 million through the offshore debt market from December 2023 to April 2024. However, the Company has moderate standby liquidity. As of 31 December 2023, the holding company had obtained total credit facilities of RMB9.0 billion from diversified domestic policy banks and commercial banks, with available amount of RMB1.4 billion. Furthermore, the Company has large amount of restricted assets, which would limit its financing flexibility. As of 31 December 2023, the Company had pledged assets of RMB6.4 billion for loans, accounting for 20.7% of total assets.

External Support

Moderate likelihood of support from the Jingdezhen Municipal Government

We expect Jingdezhen Hesheng has a moderate likelihood of receiving support from the Jingdezhen Municipal Government and its parent company in times of need. This expectation incorporates our considerations of the Company's (1) ultimate control by the Jingdezhen Municipal Government; (2) significance in promoting the strategic development of emerging industries in Jingdezhen City; and (3) solid track record of receiving support from the local government and its parent company, including subsidies, capital injections and asset transfers.

Jingdezhen SASAC maintains a high degree of control over Jingdezhen Hesheng's operations, including the formulation of business strategies and the appointment of the board of directors and key management personnel. The Company is also required to report its annual budget, objectives, plans and performance to Jingdezhen SASAC.

As the strategic industrial investment platform under the management of JSAH, the Company is one of the important subsidiaries of JSAH, assuming the role of cultivating local emerging industries in Jingdezhen City, such as aviation, new energy, and new materials. As of 31 December 2023, its consolidated assets amounted to RMB35.5 billion, accounting for 28.2% of JSAH's total assets.

Jingdezhen Hesheng receives solid support from the Jingdezhen Municipal Government and JSAH, given its strategic and economic importance in industrial investment in Jingdezhen City. In 2022, the Management Committee of Jingdezhen HIDZ has injected capitals of RMB978 million to the Company. In 2021, JSAH transferred 100% equity interests of Fengshushan Forestry to the Company, increasing its capital reserve by approximately RMB7.3 billion. From 2021 to 2023, the local government has provided subsidies of RMB1.7 billion to the Company to support its operations. The local government has also provided special funds to support the Company's construction projects and JSAH has provided guarantees to facilitate its financing. Given its strategic position in the industrial development of Jingdezhen City, we believe that the local government and shareholder will continue to provide support to the Company.

Rating Methodology

The methodology used in this rating is the Rating Methodology for [Investment Holding Companies \(December 2016\)](#).

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