

Credit Opinion

21 October 2024

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

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Weifang Guokong Development Group Co., Ltd.

Initial credit rating report

CCXAP assigns first-time long-term credit rating of BBB_g to Weifang Guokong Development Group Co., Ltd., with stable outlook.

Summary

The BBB_g long-term credit rating of Weifang Guokong Development Group Co., Ltd. (“WFGK” or the “Company”) reflects Weifang Municipal Government’s very strong capacity and the local government’s high willingness to provide support to the Company, based on our assessment of the Company’s characteristics.

Our assessment of Weifang Municipal Government’s capacity to support reflects Weifang City’s status as the fourth largest city in Shandong Province by gross regional product (“GRP”) and general budgetary revenue, with good economic and industrial development. However, Hanting District’s economic and financial strength is relatively weak, with a high regional debt pressure.

The rating also reflects the local government’s willingness to support, which is based on the Company’s (1) main infrastructure construction entity in Weifang City, especially in Hanting District; and (2) good track record of receiving government support.

However, the rating is constrained by the Company’s (1) rapid debt growth driven by ongoing investment in infrastructure construction projects; (2) weak asset liquidity and relatively high recovery risk on its account receivables; and (3) high external guarantee risk, with exposure to financially distressed enterprises.

The stable outlook on WFGK’s rating reflects our expectation that the local government’s capacity to support will remain stable, and the Company will maintain its important position in regional development of Weifang City over the next 12-18 months.

Rating Drivers

- Main infrastructure construction entity in Weifang City, especially in Hanting District
- Good track record of receiving government support
- Low exposure to commercial activities
- Rapid debt growth driven by ongoing investment in infrastructure construction projects
- Weak asset liquidity and relatively high recovery risk on its account receivables
- Fair access to funding with high concentration on bank loans
- High external guarantee risk, with exposure to financially distressed enterprises

Rating Sensitivities

What could upgrade the rating?

The rating could be upgraded if (1) Weifang Municipal Government's capacity to provide support strengthens; or (2) the Company's characteristics change in a way that strengthens the local government's willingness to provide support, such as increased strategic significance, improved debt management, strengthened funding ability, or lower exposure to contingent liability risk.

What could downgrade the rating?

The rating could be downgraded if (1) Weifang Municipal 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, deteriorated debt management, or weakened funding ability.

Key Indicators

	2021FY	2022FY	2023FY	2024Q1
Total Asset (RMB billion)	45.4	47.3	47.0	49.9
Total Equity (RMB billion)	35.6	36.1	36.5	39.2
Total Revenue (RMB billion)	2.9	2.2	2.1	0.2
Total Debt/Total Capital (%)	5.8	13.2	13.8	12.7

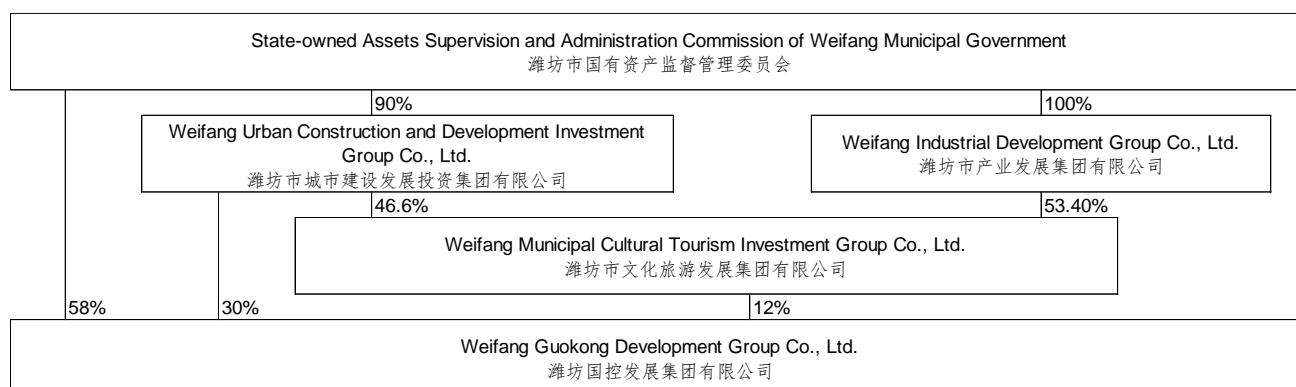
All ratios and figures are calculated using CCXAP's adjustments.

Source: Company data, CCXAP research

Corporate Profile

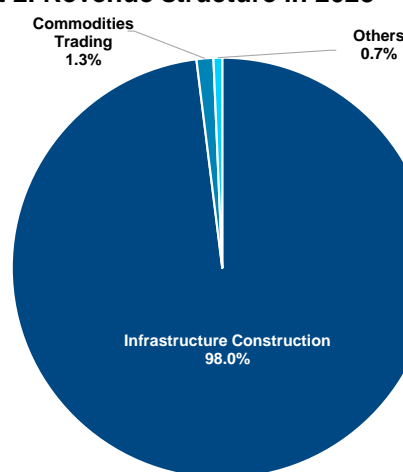
Established in 2007, WFGK became one of the main infrastructure construction entities in Weifang City after consolidation of several local state-owned enterprises in December 2022. The Company primarily focuses on the infrastructure construction, land demolition and relocation, urban renewal. It also participates in commercial activities, such as commodities trading, provision of guarantee services, and property leasing. Its businesses cover mainly in Weifang City's Hanting District and Economic Development Zone. As of 31 March 2024, the State-owned Assets Supervision and Administration Commission of Weifang Municipal Government ("Weifang SASAC") is the ultimate controller of WFGK and owned 96.4408% of the Company's shares directly and indirectly.

Exhibit 1. Shareholding chart as of 31 March 2024



Source: Company information, CCXAP research

Exhibit 2. Revenue structure in 2023



Source: Company information, CCXAP research

Rating Considerations

Government's Capacity to Provide Support

We believe Weifang Municipal Government has a very strong capacity to provide support given its status as the fourth largest city in Shandong Province by GRP and general budgetary revenue, with good economic and industrial development, but relatively tight regional refinancing pressure. Moreover, Hanting District's economic and financial strength is relatively weak, with a high regional debt pressure.

Shandong Province is the third largest province in terms of GRP in China over the past three years, with a solid industrial foundation in logistics, shipbuilding, and marine technology, chemical, automotive and agri-food. Shandong Province recorded a GRP of RMB8.7 trillion in 2022. In 2023, Shandong Province's GRP further increased to RMB9.2 trillion, a year-over-year ("YoY") increase of 6.0%. At the same time, it recorded a general budgetary revenue of RMB746.5 billion, representing a YoY increase of 5.1%.

Weifang City is located in the east-central part of Shandong Province and is an important regional economic center of central Shandong. After years of development, Weifang City has established a series of traditional advantageous industries, including power equipment, high-end chemicals, food processing, automobile manufacturing, textiles and clothing, as well as intelligent agricultural machinery. Meanwhile, Weifang City also

actively cultivates emerging industries such as new generation information technology, industrial machine tools, and magnetic levitation. In 2023, Weifang City reported a GRP of RMB760.6 billion, a YoY increase of 5.1%, ranking the 4th among prefecture-level cities in Shandong Province. In addition, Weifang City has a strong fiscal base. It reported a general budgetary revenue of RMB60.8 billion in 2023, ranking the 4th among prefecture-level cities in Shandong Province. Tax revenue accounted for 67.5% of its general budgetary revenue, on average, over the past three years. It also reported a good fiscal balance as seen by a high general budgetary revenue to general budgetary expenditure of 71.7%, on average, from 2021 to 2023.

However, Weifang City's government debt level is high, with an outstanding amount of RMB235.9 billion as of 31 December 2023, which accounted for 31.0% of its GRP. The enlarged local government debt level, together with rapidly increasing local state-owned enterprise ("SOE") debts at county level, has made Weifang City experience a tight financing environment and heightened funding costs for local SOEs since 2021. Recently, Weifang City was benefited by the strong policy support from its higher-tier government to resolve local debt risks via a package of debt-relief measures at the national level. For example, Weifang Municipal Government has obtained special refinancing fund of RMB19.6 billion in 2023, representing 70% of Shandong Province's quota for the year. We believe that Weifang City's short-term liquidity risk has decreased, but to maintain its fiscal health in the medium to long term, the city still needs to implement ongoing debt management and debt-relief measures.

Exhibit 3. Key Economic and Fiscal Indicators of Weifang City

	2021FY	2022FY	2023FY
GRP (RMB billion)	701.1	730.6	760.6
GRP Growth (%)	9.7	3.7	5.1
General Budgetary Revenue (RMB billion)	65.7	60.8	60.8
General Budgetary Expenditure (RMB billion)	88.0	84.2	88.9
Local Government Debt (RMB billion)	167.3	191.0	235.9

Source: Weifang Municipal Government, CCXAP research

Hanting District is one of the four administrative districts of Weifang City, which has jurisdiction over Weifang Economic Development Zone and Yangjiabu Tourism Development Zone. However, Hanting District's economic and financial strength is relatively weak. In 2023, it reported a GRP of RMB27.8 billion, a YoY increase of 2.0%. Hanting District Government has recorded a continuous decline on general budgetary revenue over the past three years, which decreased from RMB2.7 billion in 2021 to RMB2.1 billion in 2023. Moreover, Hanting District bears relatively high regional debt pressure. As of 31 December 2023, the outstanding government debt of Hanting District was RMB14.1 billion, accounting for 50.6% of GRP. Weifang Economic Development Zone is a provincial economic development zone in Shandong Province and plays as an important node for Weifang City's northward development.

Government's Willingness to Provide Support

Main infrastructure construction entity in Weifang City, especially in Hanting District

WFGK is one of the main infrastructure construction entities in Weifang City after consolidation of several local state-owned enterprises in December 2022. The Company primarily focuses on the infrastructure construction in Hanting District and Economic Development Zone, land demolition and relocation in Economic Development Zone, as well as the urban renewal in Hanting District. The Company generally conducts infrastructure construction through agent construction model and self-operation model, which could promote the regional development of Weifang City and Hanting District.

Under agent construction model, WFGK and its subsidiaries signed agent construction agreements with a Weifang City's entrusting party, namely Weifang Runze Greening Co., Ltd. ("Runze Green"), which is a local SOE in Weifang City controlled by Weifang Municipal Government. According to the agreement, the Company is responsible for financing and construction of the infrastructure projects, and Runze Green would pay the Company the construction costs plus a certain markup annually. WFGK has completed a large scale of infrastructure projects. As of 31 March 2024, WFGK had received project payments of RMB6.2 billion through asset transfer from the government and the remaining project payments of RMB714.9 million are expected to be paid by cash. Currently, the Company does not have agent construction projects under construction and planning.

Under self-operation model, WFGK is responsible for the financing and construction of self-operated projects and achieves fund balancing through operating income, sale, leasing and utility supplies. As of 31 March 2024, the Company had 2 self-operated projects under construction and 3 self-operated projects under planning including urban renewal, industrial park and high standard farmland. The total investment amount was RMB10.9 billion for these projects, with an uninvested amount of RMB4.9 billion. One of the largest self-operated projects of the Company, by investment scale, is Weifang Municipal Hanting Old Industrial Area Urban Renewal Project (also called "Central Business District Project"), which aims to develop high-end service industries and enhance the regional competitiveness of Weifang City. The project has obtained loans from China Development Bank with total credit facilities of RMB6.5 billion. As of 31 March 2024, the Company also received government special fund of RMB271 million to support the construction of this project.

Although the large number of infrastructure construction projects could maintain the business sustainability of WFGK, it causes large capital expenditure pressure. Moreover, the fund balancing cycle of self-operated projects is long and revenue income incurred by self-operation projects bears high uncertainty, which may further increase the Company's financial burden.

Low exposure to commercial activities

Apart from public services, WFGK also participates in commercial activities such as commodities trading, provision of guarantee services, and property leasing. We consider WFGK's commercial business exposure to be low, as the assets in commercial activities accounted for less than 15% of the total assets as 31 March 2024.

WFGK engages in commodities trading generally through sales-orient procurement model. The main products of commodities trading are seamless steel pipes, rebars, coils and hot-rolled strip. The revenue from commodities trading sharply decreased from RMB1.3 billion in 2021 to RMB26.8 million in 2023 driven by reduction of non-ferrous trade in 2022. Moreover, the gross profit margin of commodities trading is low, with 0.62% in 2023. Additionally, there is a high concentration on both upstream suppliers and downstream customers.

The Company conducts guarantee business through its subsidiary Weifang Guoke Financing Guarantee Co., Ltd. ("GKFG"), which was transferred by the local government in 2022. GKFG provides loan guarantees for micro and small-scale enterprises, agricultural entities, entities in rural areas, and farmers in Weifang City, and most guarantees have no collateral. As of 31 March 2024, GKFG had an outstanding external guarantee of RMB1.8 billion, accounting for 4.59% of WFGK's net assets. Besides, the compensation rate of GKFG's guarantee business is relatively low, at 0.19% in 2023. As of 31 March 2024, GKFG had provided compensation with accumulative amount of RMB16.5 million and collected recovery amount of RMB596 thousand. GKFG has discussed subsequent recovery measures with the guarantees and has initiated the recovery procedures.

Good track record of receiving government support

As the important infrastructure construction entity in Weifang City, WFGK has a good track record of receiving government support from local government, including government subsidies, capital injection, asset and equity transfer, which could help the Company meet its policy objectives and financial obligations. Since December 2022, the local government has transferred the shares of other local SOEs to WFGK to enlarge the Company's asset scale and capital strength. Since February 2023, the Finance Bureau of Weifang City has allocated funds to Hanting District Government, and the Finance Bureau of Hanting District has transferred the municipal government's capital injection of around RMB484.7 million to the Company. From 2021 to 2024Q1, WFGK has received government subsidies of RMB186 million in total to support its operation. In 2023, the Company received government special fund of RMB271 million to support the construction of Central Business District Project. Considering WFGK's important regional role in the development of Weifang City and Hanting District, we expect that the Company will continue to receive government support over the next 12 to 18 months.

Rapid debt growth driven by ongoing investment in infrastructure construction projects

Due to the ongoing financing for its infrastructure construction projects, WFGK demonstrated rapid debt growth. The Company's total debt increased to RMB5.7 billion as of 31 March 2024 from RMB2.2 billion as of 31 December 2021. The Company bears high short-term debt pressure as its short-term debt accounted for 41.5% of total debt at the end of March 2024. Given WFGK's uninvested amount of RMB4.9 billion from infrastructure construction projects, we estimate that the Company's total debt will continue to grow in the next 12 to 18 months.

Weak asset liquidity and relatively high recovery risk for its account receivables

WFGK's asset liquidity is weak. Its assets are comprised mainly of infrastructure assets and long-term equities in other local SOEs transferred by the government, which are considered illiquid and non-realizable and may undermine its financial flexibility. The inventory, long-term equity investment and other equity instruments accounted for around 89% of its total assets as of 31 March 2024. The inventory mainly consisted of the construction costs of infrastructure construction projects, while long-term equity investment and other equity instruments are mainly the shares of local SOEs.

Moreover, the Company also bears high recovery risk for its account receivables. As of 31 March 2024, the outstanding amount of other account receivables to Weifang Bincheng Investment Development Co., Ltd. ("BCID") was RMB1.2 billion. BCID has been listed as dishonest debtors with outstanding overdue payment of RMB430 million for commercial bills as of 30 September 2024. Moreover, BCID's subsidiaries has outstanding overdue payment for bank loans.

In addition, the Company's subsidiary Weifang National High-tech Industrial Park Co., Ltd. ("WNHT") has outstanding overdue payment of RMB9.7 million for the commercial bills as of 30 September 2024. Some of the Company's associated companies (mainly local SOEs in Hanting District) also experienced liquidity issue. On 16 October 2024, the Hanting District Government agreed to terminate the transfer of the equity of WHNT to WFGK, and WNHT would no longer be the Company's subsidiary and still be wholly held by Weifang Teda Urban and Rural Construction Investment Co., Ltd. ("WTUR").

Fair access to funding with high concentration on bank loans

WFGK has fair access to funding mainly from bank loans. The major funding channel for the Company is bank loan, which accounted for around 65% of its total debt. The Company has built a close relationship with large

domestic banks, such as China Development Bank, Agricultural Development Bank of China, and China Bohai Bank Co., Ltd. As of 31 March 2024, the Company had obtained total credit facilities of RMB9.9 billion, with an unutilized amount of RMB6.1 billion, indicating sufficient standby liquidity. The Company's financing needs may be partially released by its sufficient bank facilities. Moreover, the Company obtained lending from local SOEs in Hanting District, namely BCID and WTUR, to support its infrastructure construction. As of 31 March 2024, the outstanding lending amount from local SOEs was around RMB1.8 billion, accounting for around 30% of total debt. The Company's exposure to non-standard financing products is minor, accounted for less than 5% of its total debt. The Company plans to issue onshore and offshore bonds to expand its funding channels.

High external guarantee risk, with exposure to financially distressed enterprises

The credit profile of WFGK is constrained by its external guarantees to local SOEs and private-owned enterprises. Although the scale of external guarantees is moderate, some guarantees are in tight liquid and financial difficulty. Moreover, most of guarantees of guarantee business are private-owned enterprises, which could cause higher contingent liability risk.

In addition, the Company also provides external guarantees to local SOEs. As of 31 December 2023, the total amount of external guarantees to local SOEs was RMB713 million, which accounted for 1.95% of its net assets. The major external guarantees are provided to BCID with an outstanding amount of RMB515 million. BCID has tight liquidity and outstanding overdue payment for commercial bills. The Company had not yet incurred compensation for its guarantees to BCID as of 31 March 2024. We consider WFGK has relatively large contingent liability risk due to external guarantees to local SOEs and private-owned enterprises.

ESG Considerations

WFGK is exposed to environmental risks through its infrastructure construction projects. Such risks could be moderated through environmental studies and detailed planning prior to the start of the projects and close supervision during construction.

WFGK bears social risks as it implements public policy initiatives by undertaking infrastructure construction in Weifang 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.

WFGK's governance considerations are also material as the Company is subject to oversight and reporting requirements of the local government, 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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