

Credit Opinion

28 October 2024

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

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Mengcheng Development Zone Xingmeng Investment Co., Ltd.

Surveillance credit rating report

CCXAP affirms Mengcheng Development Zone Xingmeng Investment Co., Ltd.'s long-term credit rating to BBB_g-, with stable outlook.

Summary

The BBB_g- long-term credit rating of Mengcheng Development Zone Xingmeng Investment Co., Ltd. ("XMIC" or the "Company") reflects (1) Mengcheng County Government's relatively 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 Mengcheng County Government's capacity to provide support reflects its ongoing economic growth, but constrained by its relatively weak fiscal metrics.

The rating also reflects the local government's willingness to provide support, which is based on the Company's (1) 100% direct ownership by the Mengcheng County Government; (2) important role in the infrastructure construction and industrial development in Mengcheng County; and (3) good track record of receiving government support.

However, the rating is constrained by the Company's (1) medium exposure to commercial activities; (2) increasing debt level to support ongoing investment in construction projects; and (3) medium exposure to contingent liabilities.

The stable outlook on XMIC's rating reflects our expectation that Mengcheng County Government's capacity to provide support will remain stable, and that the Company will maintain its important position in the development of Mengcheng County over the next 12 to 18 months.

Rating Drivers

- Important role in the infrastructure construction and industrial development in Mengcheng County
- Medium exposure to commercial activities
- Good track record of receiving government support
- Increasing debt level to support ongoing investment in construction projects
- Access to multiple funding channels
- Medium exposure to contingent liabilities

Rating Sensitivities

What could upgrade the rating?

The rating could be upgraded if (1) Mengcheng County Government's ability 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 reduced exposure to risk commercial activities and improved access to funding.

What could downgrade the rating?

The rating could be downgraded if (1) Mengcheng County 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 material deteriorated debt management.

Key Indicators

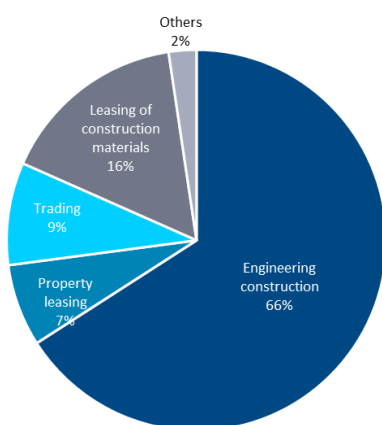
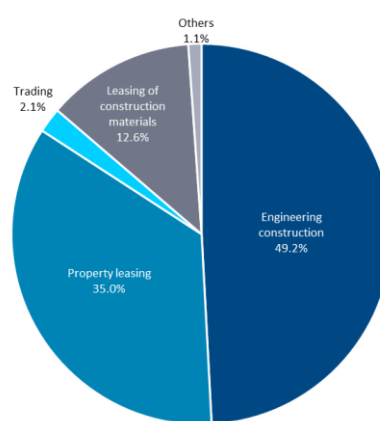
	2021FY	2022FY	2023FY	2024H1
Total Asset (RMB billion)	6.2	8.0	10.0	10.5
Total Equity (RMB billion)	4.0	4.3	4.5	4.5
Total Revenue (RMB billion)	0.5	0.8	0.7	0.2
Total Debt/Total Capital (%)	33.6	41.9	52.4	53.8

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

Source: Company data, CCXAP research

Corporate Profile

Founded in 2017, XMIC is one of the core local infrastructure investment and financing companies ("LIIFCs") in Mengcheng County. The Company is engaged in diversified businesses, such as sales of land quotas, engineering construction, property leasing, sales of construction materials, and leasing of construction materials. As of 30 June 2024, the Mengcheng County Finance Bureau was the ultimate controller of XMIC, directly holding 100% shares of the Company.

Exhibit 1. Revenue structure in 2023**Exhibit 2. Gross profit structure in 2023**

Source: Company information, CCXAP research

Rating Considerations

Government's Capacity to Provide Support

We believe that the Mengcheng County Government has a relatively strong capacity to provide support to the Company, given its ongoing economic growth, but constrained by its relatively weak fiscal metrics.

Bozhou City is a prefecture-level city in northwestern Anhui Province and the hinterland of the Huanghuai Plain. It is one of the cities in the Strategy for integrated development of the Yangtze River Delta. Its pillar industries include Chinese medicine, liquor and agricultural products processing, automobile and parts manufacturing, and cultural tourism. The economic strength of Bozhou City was at the median level among provincial-level cities in Anhui Province, but continued to improve steadily in recent years with growth rates higher than that of Anhui Province. In 2023, its gross regional product ("GRP") increased to RMB221.6 billion from RMB210.2 billion in 2022. In the first half of 2024, it achieved GRP of RMB115.7 billion with a year-on-year ("YoY") growth rate of 5.4%. Meanwhile, the general budgetary revenue of Bozhou Municipal Government increased from RMB14.8 billion in 2022 to RMB16.0 billion in 2023. The fiscal balance ratio of the Bozhou Municipal Government remained moderate. In 2023, the fiscal balance ratio (calculated by general budgetary revenue/general budgetary expenditure) was 40.8%. The debt profile of the Bozhou Municipal Government is relatively weak. At the end of 2023, the government debt balance increased to RMB98.6 billion, accounting for around 43.7% of GRP.

Exhibit 3. Key economic and fiscal indicators of Bozhou City

	2021FY	2022FY	2023FY
GRP (RMB billion)	197.3	210.2	221.6
GRP Growth (%)	8.6	4.2	6.3
General Budgetary Revenue (RMB billion)	14.0	14.8	16.0
General Budgetary Expenditure (RMB billion)	37.7	38.5	41.3
Local Government Debt (RMB billion)	72.6	83.9	98.6

Source: Bozhou Municipal Government, CCXAP research

Mengcheng County is located in the Southeast of Bozhou City, which is also within the coverage of the integrated planning of the Yangtze River Delta, and enjoys favorable conditions for economic development. Besides, Mengcheng County enjoys abundant natural resources such as mineral and coal resources. It is a

large producer of agricultural products such as high-quality wheat, corn, yam, cotton, and rapeseed. In accordance with the report of CCID Consulting, Mengcheng County has been ranked in the list of “Top 100 Counties (Cities) for Business Environment” in 2019, “Top 100 Counties in the Yangtze River Delta” in 2022 and “Top 100 Counties in Central China” in 2023. The leading industries in Mengcheng County include automobile and equipment manufacturing, new building materials and household products, food manufacturing and agricultural products processing. In 2023, Mengcheng County’s GRP amounted to RMB48.0 billion, ranking second among four divisions in Bozhou City, with a YoY growth rate of 6.1%. In the first half of 2024, Mengcheng County’s GRP reached RMB25.5 billion with a YoY growth rate of 6.1%. Mengcheng County Government’s general budgetary revenue increased to RMB2.9 billion in 2023 from RMB2.8 billion in 2022. However, its fiscal balance ratio remained moderate at 40.8% in 2023, reflecting a high reliance on fiscal support from higher-tier governments and proceeds from land sales to balance its fiscal budget. As of 31 December 2023, the outstanding debt of Mengcheng County Government increased to RMB21.0 billion, accounting for 43.7% of its GRP.

Exhibit 4. Key economic and fiscal indicators of Mengcheng County

	2021FY	2022FY	2023FY
GRP (RMB billion)	42.9	45.9	48.0
GRP Growth (%)	8.7	4.4	6.1
General Budgetary Revenue (RMB billion)	2.6	2.8	2.9
General Budgetary Expenditure (RMB billion)	6.7	7.0	7.2
Local Government Debt (RMB billion)	15.0	17.8	21.0

Source: Mengcheng County Government, CCXAP research

Mengcheng ETDZ was established in 2001 and approved as a provincial-level Economic and Technological Development Zone in 2006. It has formed three leading industries including automobile and machinery manufacturing, agricultural and sideline products processing, light textile manufacturing. Mengcheng ETDZ has more than 1,000 enterprises, of which 121 are large-scale industrial enterprises, 45 are high-tech enterprises, and 32 are strategic emerging enterprises. From January to July 2024, the total industrial output value of Mengcheng ETDZ has exceeded RMB10 billion, up 13.5% YoY. We believe the population agglomeration effect formed along with the continuous improvement of related industrial chains will promote the further development of the Mengcheng ETDZ.

Government’s Willingness to Provide Support

Important role in the infrastructure construction and industrial development in Mengcheng County

XMIC is one of the core LIIFCs in Mengcheng County and is directly owned by the local government. The Company plays an important role in the industrial and economic development of Mengcheng County, especially the Mengcheng County Economic Development Zone, through largely contributing to the local infrastructures and capital attraction. The Company has introduced number of enterprises to Mengcheng County through the construction of industrial parks, forming an important contribution to the local government’s tax revenue.

XMIC’s infrastructure construction business mainly includes the urban and rural construction land increase and decrease linked projects in Mengcheng County. These projects aim to increase the urban construction land by consolidating the rural arable land. According to the agreement signed with the Mengcheng Natural Resources and Planning Bureau in 2020, the Company undertakes the vacation and reclamation of homesteads in 17 townships and street offices in Mengcheng County and the project cycle is 7 years. The Company is responsible for the construction management of the project, including financing, management of construction funds, land

acquisition and relocation and infrastructure construction. However, at present, the Company has no related project under construction or planning, demonstrating moderate business sustainability for this segment.

Medium exposure to commercial activities

XMIC is engaged in diversified commercial activities including engineering construction, trading, and leasing of construction materials. While the commercial activities generate supplemental income to the Company, they may entail higher operational and business risks than public policy activities. Based on our estimates, the Company had medium exposure to commercial activities, which accounted for around 30% of its total assets.

XMIC is engaged in engineering construction through its subsidiary and construction projects are mainly within Mengcheng County acquired through tender invitations and public bidding. The engineering construction business is the main income driver of the Company, accounting for around 65.9% of total revenue in 2023 with a gross profit margin of 14%. The main customers in recent years are government, state-owned enterprises, as well as enterprises settled in Mengcheng County. As of 30 June 2024, the Company had a total contract value of RMB1.2 billion in hand, indicating good business stability. However, the engineering construction business has a relatively long construction period and slow repayment collection, which brings certain pressure on repayments during the downturn in the construction industry.

The Company is also involved in the property leasing business, mainly including factories. As of 30 June 2024, the Company owned rental properties with a total book value of RMB1.8 billion and an average occupancy rate of 66%, providing supplementary income to the Company. XMIC has also conducted the construction and operation of self-owned projects, including industrial parks and rental housing, aiming to support local industries and supplement its income. The Company plans to achieve fund balance through sale or lease. The Company has a large investment in the construction of industrial parks. As of 30 June 2024, the Company had 2 projects under construction, with a total planned investment of RMB259.3 million and an uninvested amount of RMB9.3 million. The Company also has 5 proposed projects with a total planned investment of RMB2.5 billion. These proposed projects are planned to be carried out in phases, which could alleviate the pressure on funding requirements. With the completion of projects, we expect the leasable properties and rental income of the Company will increase, which also increase its commercial risk exposure. However, these self-construction projects are highly related to local industrial development and the progress of investment attraction, which may bring greater uncertainties to the Company.

XMIC conducts trading business through its subsidiary in the form of import, export, wholesale and retail (including supply chain business), accounting for around 8.7% of total revenue in 2023. Trading products mainly include clothing and textiles. Benefiting from enriching products of export sector, the revenue scale of trading business achieved fast growth in 2023, up 78.5% YoY. However, the gross profit margin of this business has remained low at 2.1% in 2023. Meanwhile, there is a high concentration risk regarding to upstream suppliers and downstream customers. For the first half of 2024, the top two suppliers accounted for 89% of the total procurement and the sales from the top five customers accounted for around 69% of the total sales.

The Company's leasing of construction materials business primarily procures projects through bidding. It signs leasing contracts with downstream construction companies based on the project obtained. The reserve of aluminum templates and other building materials basically meets the Company's leasing needs at the present time and the demand is expected to increase due to the improving local property market. The revenue of leasing of construction materials business increased from RMB98.1 million in 2022 to RMB113.6 million in 2023, up 15.8% YoY, accounting for around 16% of total revenue in 2023.

Moreover, the Company is also responsible for security business in Mengcheng County. The security business mainly provides labor dispatch and security services within industrial parks the Company operates. This business contributes less to the Company's overall revenue as it accounted for less than 5% of the Company's total revenue in 2023.

Solid track record of receiving government support

As one of the core LIIFCs of Mengcheng County, XMIC has a good track record of receiving support from the local government in the form of asset injections, capital injections and government subsidies to support its operation. From 2021 to 2023, the Company received capital injection of RMB890.7 million in cash and paid-in capital of RMB922 million from the Mengcheng County Finance Bureau, substantially enhancing its capital strength. The Company also received property assets with evaluation value of RMB369.1 million in 2021 and property assets with evaluation value of RMB15.5 million in 2023 without compensation. From 2021 to 2023, the Company continuously received government subsidies with a total amount of around RMB636.2 million, including fiscal and operating subsidies, which support its future investments and debt repayments. Given the Company's important position and its close relationship with the local government, we expect that the Company will continue to receive support from the local government.

Increasing debt level to support ongoing investment in construction projects

Due to the continuous investment in construction projects, XMIC shows a rising debt burden over the past few years. As of 30 June 2024, the Company's total debt increased to RMB5.3 billion from RMB3.1 billion at end-2022. The Company's capitalization ratio increased from 41.9% to 53.8% during the same period. At the same time, the Company's short-term debt accounted for around 30.0% of total debt and the cash to short-term debt ratio was around 0.6x, indicating refinancing needs for its short-term debt. Given the Company's future capital expenditure pressure for its investment and construction projects, we expect the Company's debt level will continue to increase for the next 12-18 months.

Moderate asset liquidity

XMIC's asset liquidity is moderate. As of 30 June 2024, its account receivables, other receivables and inventories accounted for around 59.4% of total assets. The Company's inventories mainly include land assets and the cost of construction works, while receivables are mainly receivables from the local government, which are considered low liquidity. On top of that, as of 30 June 2024, the Company's investment properties accounted for around 16.7% of the total assets, providing supplementary income to the Company.

Access to multiple funding channels

XMIC has multiple access to funding, including bank loans and bond issuance, with a comprehensive financing cost at about 5.2%. As of 30 June 2024, bank loans accounted for 73.8% of total debt. The Company maintains long-term relationships with different large domestic banks including large state-owned commercial banks and joint-stock commercial banks. As of 30 June 2024, the Company had total bank facilities of RMB7.4 billion, with the available portion being RMB3.3 billion. In addition, the Company expanded its funding channels by issuing two tranches of offshore bonds in July and August 2023 to raise a total of RMB810.0 million. The Company also plans to broaden its financing channels by issuing onshore bonds. Meanwhile, the Company has a low exposure to non-standard financing, such as financial leasing, which accounted for around 10.9% of its total debt. We consider the Company's diversified funding channels can largely fulfill its future capital expenditure and refinancing needs.

Medium exposure to contingent liabilities

XMIC's credit profile is constrained by its external guarantees, which could potentially increase its repayment obligations. As of 30 June 2024, the Company had external guarantees of RMB2.1 billion, accounting for around 47.0% of its net assets, which exposes the Company to substantial contingent liabilities. The guarantees are provided to other LIIFCs in Mengcheng County. In case a credit event occurs, the Company may face large-scale cross-effects risks, which could negatively impact its credit quality. Nevertheless, we believe that the contingent risk of the external guarantee is moderately controllable, considering the position of these state-owned enterprises and may receive timely support from the local government.

ESG Considerations

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

XMIC bears social risks in implementing public policy initiatives through the building of public infrastructure in Mengcheng County. 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.

XMIC's governance considerations are also material as the Company is subject to oversight by the Mengcheng County Government and must 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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