

Credit Opinion

11 November 2024

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

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Luzhou High-tech Investment Group Co., Ltd.

Surveillance credit rating report

CCXAP affirms Luzhou High-tech Investment Group Co., Ltd.'s long-term credit rating at BBB_g-, with stable outlook.

Summary

The BBB_g- long-term credit rating of Luzhou High-tech Investment Group Co., Ltd. ("LHIG" or the "Company") reflects Luzhou Municipal Government's (1) very strong capacity to provide support, and (2) relatively high willingness to provide support based on our assessment of the Company's characteristics.

Our assessment of Luzhou Municipal Government's capacity to support reflects Luzhou City's status as an important trade and logistics center in the Chengdu-Chongqing Economic Circle and a well-known domestic alcohol industry base, with growing economic and fiscal strengths. Meanwhile, Luzhou High-Tech Industrial Development Zone ("Luzhou High-Tech Zone") is a National High-Tech Industrial Development Zone with pillar industries including high-end manufacturing and modern service.

The rating also reflects the local government's willingness to support, which is based on the Company's (1) key role in the infrastructure construction and high-tech industry investment in Luzhou High-tech Zone; (2) solid track record of receiving government support; and (3) access to funding from banks and bond markets.

However, the Company's rating is constrained by its (1) relatively low sustainability of public projects; (2) medium exposure to commercial activities; (3) high debt leverage with relatively high debt repayment pressure; and (4) high contingent risk arising from external guarantees.

The stable outlook on LHIG's rating reflects our expectation that the Luzhou Municipal Government's capacity to provide support will remain stable, and the Company's characteristics such as its key role in infrastructure construction in the High-Tech Zone will remain unchanged over the next 12 to 18 months.

Rating Drivers

- Key role in the infrastructure construction and high-tech industry investment in Luzhou High-Tech Zone
- Solid track record of receiving government support
- Good access to funding from banks and bond markets
- Relatively low sustainability of public projects
- Medium exposure to commercial activities
- High debt leverage with relatively high debt repayment pressure
- High contingent risk arising from external guarantees

Rating Sensitivities

What could upgrade the rating?

The rating could be upgraded if (1) Luzhou Municipal Government's capacity to support strengthens; and (2) the Company's characteristics change in a way that strengthens the local government's willingness to support such as materially reduced exposure to risky commercial activities and improved debt management.

What could downgrade the rating?

The rating could be downgraded if (1) Luzhou Municipal Government's capacity to support weakens; or (2) the Company's characteristics change in a way that weakens the local government's willingness to provide support, such as weakened market position, deteriorated access to fundings, or material decreased government support.

Key Indicators

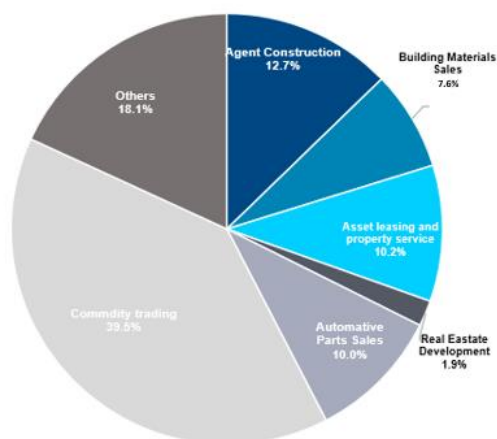
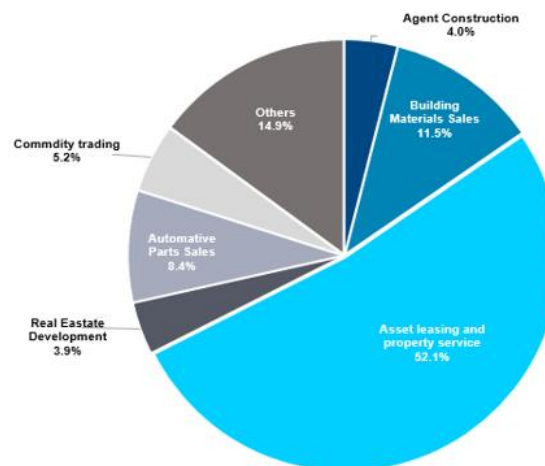
	2021FY	2022FY	2023FY	2024Q1
Total Asset (RMB billion)	20.4	21.4	24.5	25.8
Total Equity (RMB billion)	6.3	6.5	7.9	7.9
Total Revenue (RMB billion)	1.9	2.5	2.2	0.7
Total Debt/Total Capital (%)	67.1	67.6	66.2	67.8

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

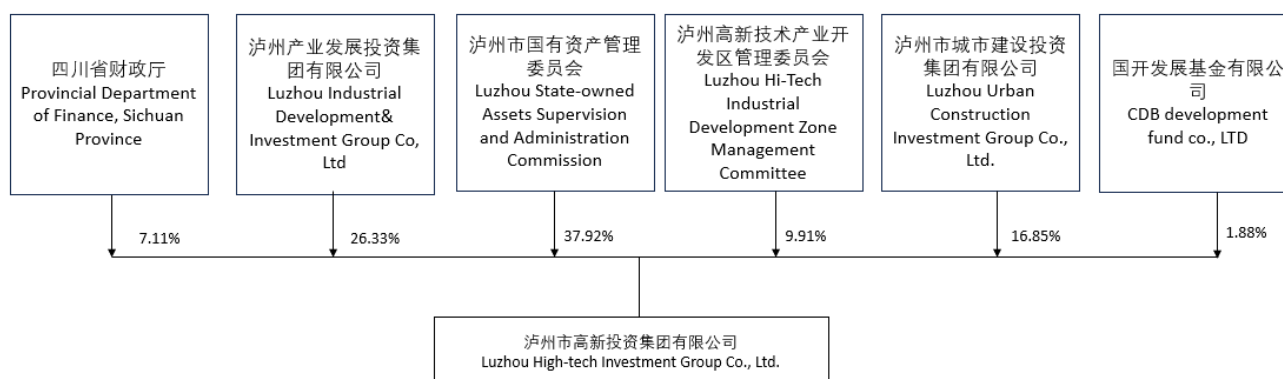
Source: Company information, CCXAP research

Corporate Profile

Established in December 2013, LHIG is the sole entity responsible for local infrastructure construction in the Luzhou High-Tech Zone and the sole state-owned high-tech industry investment entity in Luzhou City. The Company is also engaged in businesses such as self-operated project construction and leasing, real estate development, sales of energy, and building materials sales. As of 31 March 2024, the largest shareholder and the actual controller of the Company was the Luzhou State-owned Assets Supervision and Administration Commission ("Luzhou SASAC"), directly holding 37.92% of the shares of the Company and indirectly holding another 43.18% via Luzhou Industrial Development & Investment Group Co., Ltd. and Luzhou Urban Construction Investment Group Co., Ltd.

Exhibit 1. Revenue Structure in 2023**Exhibit 2. Gross Profit Structure in 2023**

Source: Company information, CCXAP research

Exhibit 3. Shareholding chart as of 31 March 2024

Source: Company information, CCXAP research

Rating Considerations

Government's Capacity to Provide Support

We believe that the Luzhou Municipal Government has a strong capacity to provide support, reflecting Luzhou City's status as an important trade and logistics center in the Chengdu-Chongqing Economic Circle and a well-known domestic alcohol industry base, with growing economic and fiscal strengths.

Sichuan Province is a leading economic province and is recognized as one of the most developed provinces in China. In 2023, Sichuan recorded a GRP of RMB6.0 trillion, with a year-on-year ("YoY") increase of 6.0%, ranking 5th in terms of GRP among all provinces in China. The general budgetary revenue of Sichuan increased to RMB522.9 billion in 2023, up by 13.3% YoY. In 2024H1, Sichuan recorded a GRP of RMB2.9 trillion, with a YoY increase of 5.4%.

Luzhou City is a prefecture-level city of Sichuan Province. With the solid development of industries including liquor, electronic information, energy, and chemicals, Luzhou City's economic and fiscal strength ranks in the

upper reaches of Sichuan Province. In 2023, Luzhou City's GRP was RMB272.6 billion, ranking 6th among all prefecture-level cities in Sichuan Province, representing an increase of 5.6% over the previous year. Its general budgetary revenue amounted to RMB21.2 billion in 2023, ranking 3rd among all cities in Sichuan Province, a YoY increase of 10.3%. Tax revenue accounted for around 60.6% of its general budgetary revenue in 2023, a slight increase from 2022. Meanwhile, its fiscal balance ratio was around 44.9% in 2023, which was at a moderate level. The government debt was RMB99.4 billion in 2023, representing 36.5% of its GRP. In the first half of 2024, Luzhou City recorded GRP of RMB126.5 billion, representing a YoY increase of 3.6%. Meanwhile, its general budgetary revenue increased to RMB12.9 billion, a YoY increase of 2.0%.

Exhibit 4. Key economic and fiscal indicators of Luzhou City

	2021FY	2022FY	2023FY
GRP (RMB billion)	240.6	260.2	272.6
GRP Growth (%)	8.5	4.1	5.6
General Budgetary Revenue (RMB billion)	19.0	19.3	21.2
General Budgetary Expenditure (RMB billion)	44.5	45.9	47.3
Local Government Debt (RMB billion)	72.7	86.8	99.4

Source: Statistic Bureau of Luzhou City, CCXAP research

Luzhou High-tech Zone was established in 2013 and was upgraded to a national high-tech industrial development zone with the approval of the State Council in February 2015. It is one of the three national high-tech industrial development zones in the upper reaches of the Yangtze River Economic Belt, with a total planned area of 202 square kilometers and a core area of 36 square kilometers. Luzhou High-tech Zone has several parks including the Modern Pharmaceutical Industrial Park, the High-end Equipment Manufacturing Industrial Park, the New Energy and New Materials Industrial Park, the Big Data Industrial Park as well and the Smart Grid Industrial Park. In 2023, Luzhou High-tech Zone achieved operating income of around RMB130 billion, a year-on-year increase of 9%. Luzhou Municipal Government has provided various supports to the High-tech Zone. The land quota will be given priority to the High-Tech Zone, which enjoys preferential prices. The development of the high-tech zone provides support for the long-term sustainable development of the Company.

Government's Willingness to Provide Support

Key role in the infrastructure construction and high-tech industry investment in Luzhou High-Tech Industrial Development Zone

LHIG is the sole entity responsible for local infrastructure construction in Luzhou High-Tech Zone, providing a range of services including land consolidation and pipeline construction. The Company plays a crucial role in the Luzhou High-Tech Zone, and has successfully completed a series of large-scale infrastructure projects and public welfare facilities, such as schools, landscape and greening projects. In order to attract high-quality enterprises to settle in the Luzhou High-Tech Zone, the Company's business has gradually shifted from land development and infrastructure construction to the construction of factories, office buildings and other facilities. Considering the Company's high strategic significance to the development of Luzhou High-tech Zone, we believe the Company will not be easily replaced by other local state-owned enterprises in the foreseeable future.

The infrastructure construction projects undertaken by the Company are mainly carried out through agency construction model. As of end of March 2024, the repayment progress of completed projects is relatively good. The total amount of planned repayment is RMB1.5 billion, and RMB1.3 billion has already been collected.

However, the large-scale construction of infrastructure projects in the High-Tech Zone has almost ended, and there are currently no infrastructure projects under construction or planning, demonstrating that the Company's business sustainability of public policy projects is relatively low. In addition, as of 31 March 2024, the Company had 1 infrastructure project under construction, which carries a total planned investment of RMB313.9 million and uninvested amount of RMB19.6 million. Meanwhile, there is no infrastructure project under planning.

Medium exposure to commercial activities

LHIG is also engaged in commercial activities such as self-operated construction and leasing, real estate development, sales of building materials, sales of automotive parts, and commodity trading business. Although the Company's commercial activities accounted for about 30% of its total assets in 2023, we consider the business risk in these commercial activities to be manageable, because some businesses are closely related to its strategic role in the industrial development of Luzhou High-tech Zone.

The Company's self-operated construction and leasing business mainly facilitates the investment attraction of Luzhou High-Tech Zone. The Company is responsible for building plants, data centers or office buildings based on the needs of the incoming enterprises. As of the end of March 2024, the Company had a total estimated investment amount of RMB2.5 billion and an outstanding amount of RMB764.6 million. Currently, the Company has no self-operated projects under planning. As of 31 December 2023, the Company had a total leasing area of 1.2 million square meters, providing supplementary rental income to the Company. In 2023, the revenue from asset leasing and property service further declined to RMB223 million from RMB294 million in 2022, mainly due to the low occupancy rate (2023: 46.4%). In addition, the asset leasing and property service remained a relatively high gross profit margin level of 76.7%. As the leasing business is mainly subject to the investment attraction progress of the High-Tech Zone, this business segment may face uncertainty in terms of its future cash inflow.

LHIG is engaged in property development projects through the self-construction model, including residential and commercial property development projects. Due to the slowdown of China property market, revenue from property development business declined to RMB42.3 million in 2023 (2022: RMB72.0 million). As of 31 March 2024, the Company had 2 major property development projects under construction, with a total estimated investment amount of RMB1.5 billion and an outstanding amount of RMB517 million. The Company had one completed project under sale, however, the selling rate has yet reached 50%. As the sales of real estate projects are subject to the industry downturn, the debts formed by the property development may bring certain debt repayment pressure to the Company.

LHIG's sales of building materials business mainly involves sale of concrete, sand and stone. The Company mainly establishes cooperation with large central enterprises and supplies concrete, steel and other products to their engineering projects. In 2023, the Company achieved building materials sales revenue of RMB 1.6 billion, a slight decrease from the previous year, which was mainly due to the slowdown of the project construction in the nearby region. In addition, The Company's auto parts sales business is mainly managed by its subsidiary, Luzhou Hi-Tech AVIC Transmission Steering System Co., Ltd., which mainly produces gears, input shafts, assemblies, internal and external planetary wheels and other automotive transmission system components. Though top 5 suppliers accounted for less than 40% of total procurement, this business has a relatively high customer concentration risk, since the top 5 customers account for 66.9% of total revenue.

The largest contributor to the revenue of the Company is commodity trading business, which involves the sales of woods, steel and other commodities. The segment faces high concentration risks in suppliers and customers. The top 5 suppliers and customers accounted for 100% of total procurement and sales, respectively. In 2023,

the segment recorded a revenue of RMB861 million. However, the gross margin of the segment is less than 1%, limiting its contribution to the overall gross profit. The commercial businesses the Company engages in also include energy sales, software development, and cloud service. However, their relatively small scale limited their contribution to the overall revenue.

Solid track record of receiving government support

As the Company closely ties with the Luzhou Municipal Government in terms of business operations, and investment and financing decisions, the Company has a good track record of receiving support from the local government in the past few years. These supports take various forms, such as government subsidies and capital injections. In 2023, the local government injected capital of RMB1.0 billion to the Company. As of 31 March 2024, the registered capital and paid-up capital were both RMB2.7 billion. Over the same period, the Company also received financial subsidies and interest subsidies of around RMB1.0 billion from the local government. In light of LHIG's important regional position in infrastructure construction and investment attraction of Luzhou High-Tech Zone, we expect the Company to receive ongoing support from the local government over the coming 12-18 months.

High debt leverage with relatively high debt repayment pressure

With ongoing financing for its construction projects in recent years, LHIG has a high debt leverage. The Company's total debt had increased from RMB16.5 billion at end-2022 to RMB16.6 billion as of 31 March 2024, and its total capitalization amounted to 67.8%. The Company faced relatively high short-term debt pressure as its short-term debt accounted for around 50.8% of its total debt and its cash/short-term debt remained at 0.2x as of 31 March 2024. Given the Company's capital expenditure pressure, we expect the Company will maintain a relatively high debt leverage for the next 12-18 months.

Furthermore, LHIG has moderate asset liquidity. The Company's liquid asset mainly consists of receivables, investment properties, and inventories, which accounted for 73.3% of its total asset as of 31 March 2024. Receivables are mainly unreceived payments from the agencies of the government or other state-owned companies, and inventories are mainly investment costs for its construction projects, all of which are considered low liquidity. Moreover, as of the end of 2023, the total restricted assets were RMB6.7 billion which accounted for around 26% of total assets and was mainly used for bank financing.

Access to funding from banks and bond markets

LHIG has good access to diversified funding such as bank loans and onshore bond financing, with bank loans accounting for about 51% and bonds accounting for about 26% of its total debts as of 31 March 2024. The Company has issued various types of bonds, such as MTNs, and corporate bonds in 2024, with a coupon rate ranging from 2.6% to 3.4%. The Company maintains long-term close relationships with policy banks, state-owned commercial banks, and joint-stock commercial banks, such as the Agricultural Development Bank of China and the Industrial and Commercial Bank of China. The Company held total credit facilities of RMB22.3 billion, with an unutilized amount of RMB10.2 billion as of end-2024. However, as of 31 March 2024, around 22% of the Company's total debt was non-standard financing.

High contingent risk arising from external guarantees

LHIG's credit profile is constrained by its external non-operating guarantees, which could potentially increase its repayment obligations. As of 31 March 2024, the Company had outstanding external guarantees of RMB9.8 billion, representing 123.9% of its net assets. All of them were provided to local state-owned enterprises

(“SOEs”). The Company’s contingent liabilities are subject to regional risks due to the mutual guarantee situation. Besides, the Company has lots of mutual payments with other SOEs in this region. In case a credit event occurs, the Company may face certain contingent liability risks, which could negatively impact its credit quality. However, we estimate most of these local SOEs are likely to be supported by the local government when necessary.

ESG Considerations

LHIG bears environmental risks through its infrastructure projects. Such risks could be mitigated by conducting environmental studies and detailed planning before the commencement of the projects and close supervision during construction.

LHIG bears social risks as it implements public policy initiatives by building public infrastructure in the Luzhou High-tech Zone. 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.

LHIG’s governance considerations are also material as the Company is subject to oversight by Luzhou 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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