Credit Opinion

5 December 2024

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

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Jiangsu Yungang Development Group Co., Ltd.

Surveillance credit rating report

CCXAP affirms Jiangsu Yungang Development Group Co., Ltd.'s long-term credit rating at BBB_g-, with stable outlook.

Summary

The BBB_g- long-term credit rating of Jiangsu Yungang Development Group Co., Ltd. ("Yungang Group" or the "Company") reflects Lianyungang Municipal Government's strong capacity to provide support and its high willingness to provide support based on our assessment of the Company's characteristics.

Our assessment of the local government's capacity to provide support reflects Lianyungang City's gross regional production ("GRP") of over RMB400 billion, with good industrial development and port resources. In addition, Lianyun District is a municipal district in Lianyungang City with good economic growth and fiscal metrics.

The rating also reflects the local government's willingness to provide support, which is based on the Company's (1) ultimate control by the Lianyungang Municipal Government; (2) strong policy role in the industrial development of Lianyun District, especially the Lianyun Economic and Development Zone ("Lianyun EDZ"); and (3) track record of receiving government support.

However, the rating is constrained by the Company's (1) medium commercial activities exposure; (2) moderate access to funding with limited financing flexibility; and (3) large exposure to external guarantees provided to local state-owned enterprises.

The stable outlook on Yungang Group's rating reflects our expectation that the local government's capacity to provide support will be stable; and the Company's characteristics, such as its primary role in the development of the Lianyun District and Lianyun EDZ, which is expected to remain unchanged over the next 12 to 18 months.

Rating Drivers

- Strong policy role in the industrial development of Lianyun EDZ
- Medium exposure to commercial activities
- Track record of receiving government support
- Rising debt level driven by increasing local investments
- Moderate access to funding with limited financing flexibility
- Large exposure to external guarantees provided to local state-owned enterprises

Rating Sensitivities

What could upgrade the rating?

The rating could be upgraded if (1) the local government's capacity to support materially strengthens; or (2) the Company's characteristics change in a way that strengthens the local government's willingness to support such as an increase in the importance of its policy role, improved debt management, or reduced exposure to commercial activities.

What could downgrade the rating?

The rating could be downgraded if (1) the local government's capacity to support weakens; or (2) the Company's characteristics change in a way that weakens the local government's willingness to support, such as an increase in risk exposure to commercial activities, or decline in its policy significance.

Key Indicators

	2021FY	2022FY	2023FY	2024H1
Total Assets (RMB billion)	10.1	11.3	12.2	14.3
Total Equity (RMB billion)	4.8	4.9	4.8	4.8
Total Revenue (RMB million)	701.6	741.2	704.8	346.0
Total Debt/Total Capital (%)	45.2	50.0	52.0	58.9

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

Source: Company information, CCXAP research

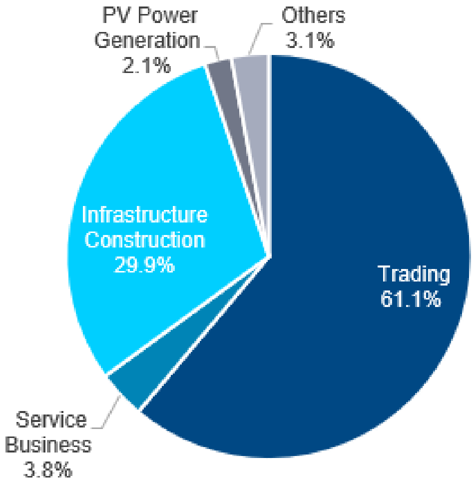
Corporate Profile

Established in 2009, Yungang Group, formerly known as Jiangsu Yungang Investment Development Co., Ltd., is the primary local infrastructure investment and financing company ("LIIFC") focusing on industrial investment in the Lianyun District, Lianyungang City. Yungang Group mainly undertakes the role of local infrastructure construction, industrial supporting projects and comprehensive services in the Lianyun EDZ, a provincial-level EDZ in the Lianyun District. The Company has developed diversified business segments, including infrastructure construction, service businesses such as sewage treatment and inland port operation, photovoltaic (PV) power generation, property leasing, and trading. As of 30 June 2024, the Company is ultimately controlled by Lianyungang Municipal Government through Jiangsu Haizhou Bay Holding Group Co., Ltd ("Haizhou Bay Holding").

Exhibit 1. Shareholding chart as of 30 June 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 that the local government has a strong capacity to provide support, given Lianyungang Municipal Government's GRP of over RMB400 billion, ranking Top 100 among all the prefecture-level cities in China. It also has good industrial development and port resources. In addition, Lianyun District is a municipal district in Lianyungang City with good economic growth and fiscal metrics. However, Lianyungang Municipal Government's fiscal metrics are moderate.

Jiangsu Province is one of the leading and well-developed provinces in China. It is home to many of the world leading enterprises of electronic equipment, chemicals, and textiles. Jiangsu Province is the second largest province in China by GRP, after Guangdong Province. In 2023, its total GRP amounted to RMB12.8 trillion, a year-over-year ("YoY") increase of 5.8%. The per capita GRP for the same period was RMB150,487, ranking first among all provinces in China. In the first three quarters of 2024, Jiangsu Province's GRP reached RMB9.7 trillion, a YoY increase of 5.7% at constant prices.

Lianyungang City is one of the first 14 Chinese coastal cities opening to the outside world and has one of the major ports of China — the Lianyun Port. With geographic advantages, it has developed port industries such as petrochemicals, ferrous metallurgy and mechanical equipment manufacturing. Lianyungang City also promotes emerging industries such as biomedical, new materials, new energy and high-end equipment industry. Rapid industrial growth supports Lianyungang City's economy to maintain growth. In 2023, Lianyungang City's GRP increased by 10.2% to RMB436.4 billion, where the growth rate ranked top among all prefectural cities in Jiangsu Province. Compared to last year, the general budgetary revenue increased to RMB25.6 billion from RMB21.3 billion with tax revenue rising to RMB19.6 billion from RMB12.7 billion. Tax contribution recovered to 76.5% in 2023 so the 3-year average fiscal stability (tax/general budget revenue) increased to 71.9%, indicating a strong revenue-generating ability. However, the fiscal sufficiency of Lianyungang Municipal Government was still relatively weak. The fiscal balance ratios (general budgetary revenue/ general budgetary expenditure) were less than 50% over the past three years, indicating high reliance on support from high-tier governments. In addition, the governmental fund revenue is an important supplement to the financial resources of the Lianyungang Municipal Government, which highly depends on the performance of land sales market. The local government's direct debt kept increasing and reached around RMB73.3 billion as of the end of 2023, accounting for about 16.8% of GRP. In the first three quarters of 2024, Lianyungang City achieved a GRP of RMB313.3 billion, a YoY increase of 5.8%.

Exhibit 3. Key economic and fiscal indicators of Lianyungang City

	2021FY	2022FY	2023FY
GRP (RMB billion)	372.8	400.5	436.4
GRP Growth (%)	8.8	2.4	10.2
General Budgetary Revenue (RMB billion)	27.5	21.3	25.6
General Budgetary Expenditure (RMB billion)	53.4	53.6	57.5
Local Government Debt (RMB billion)	65.8	68.0	73.3

Source: Lianyungang Municipal Government, CCXAP research

Lianyun District has abundant ocean and tourism resources and has been awarded as an all-for-one tourism demonstration zone since 2016. The local government has also promoted industrial development by establishing industrial parks to attract investments, such as the SCO(Lianyungang) International Logistics Park ("SCO Park") and the Lianyun EDZ, where Yungang Group mainly operates. Metal materials and chemical industries are Lianyun District's pillar industries. Lianyun District has a small economic size among county-level cities in Lianyungang City but has kept ongoing economic growth over the past few years. Lianyun District has relatively good fiscal balance and stability. In 2023, its general budgetary revenue increased to RMB2.4 billion from RMB2.2 billion in 2022. Meanwhile, the tax revenue, a stable source for Lianyun District Government's general budgetary revenue, also increased to RMB1.9 billion. The fiscal balance ratio remained at a high level of 114.2% and tax accounted for 82.5% of its budgetary revenue as of the end of 2023, representing a relatively good fiscal quality. As of the end of 2023, the Lianyun District Government's outstanding government debts slightly increased to RMB2.1 billion, which accounted for around 8.2% of GRP.

Exhibit 4. Key economic and fiscal indicators of Lianyun District

	2021FY	2022FY	2023FY
GRP (RMB billion)	25.5	25.6	28.2
GRP Growth (%)	10.2	0.8	7.0
General Budgetary Revenue (RMB billion)	2.1	2.2	2.4
General Budgetary Expenditure (RMB billion)	2.0	2.0	2.1

Local Government Debt (RMB billion)	1.8	2.1	2.3

Source: Lianyun District Government, CCXAP research

Lianyun EDZ was established in 1992 and became a provincial-level development zone in 2006. It is one of the key industrial development areas of Lianyun District and has formed an industrial cluster dominated by new energy, chemical and metal materials industry. Lianyun EDZ has attracted a number of enterprises such as Lianyungang Huale Alloy Group Co., Ltd., Jiangsu Sanjili Chemical Co., Ltd., Wilmar Polymer Materials (Lianyungang) Co., Ltd., Lianyungang Hengxintong Mining Co., Ltd. and Chinalco Jiangsu Rare Earth Co., Ltd. In 2019, mandated by the Lianyungang Municipal Government, the Management Committee of the Lianyun EDZ assumed the responsibility for the development and management of the SCO Park. SCO Park is a provincial and municipal hub for modern service industries and a key municipal logistics base. In the first half of 2024, SCO Park completed logistics flow of 289.0 million tons. Lianyun EDZ actively promotes the construction of key projects to accelerate high-quality development. For instance, the construction of Tianwan photovoltaic project, which has been included in the third batch of national large-scale photovoltaic base projects. After completion, it will become the world’s largest offshore photovoltaic power station.

Government’s Willingness to Provide Support

Strong policy role in the industrial development of Lianyun EDZ

In 2023, the local government positioned Haizhou Bay Holding as the entity to consolidate the main LIIFCs in Lianyun District, including Jiangsu Haizhou Bay Development Group Co., Ltd.(“HZDG”) and Yungang Group. Yungang Group is the key industrial investment platform that undertakes the functions of infrastructure development, industrial supporting project construction and providing comprehensive services in the Lianyun EDZ and the SCO Park, which are the key industrial parks of the Lianyun District. The success of the Lianyun EDZ and the SCO Park is important to the industrial and economic development of the Lianyun District as it contributed an important part of tax revenue and fiscal income for the region.

Yungang Group has an essential role in the development of Lianyun EDZ as seen by its large contribution to the local infrastructure construction such as roads, land consolidation, factories and resettlement housings. As of 30 June 2024, there were 7 infrastructure construction projects under construction, with a total estimated investment amount of RMB675.0 million and an uninvested amount of RMB638.0 million. Meanwhile, the Company had 3 projects under planning with an estimated investment amount of RMB100.0 million. Yungang Group is also involved in commercial activities to support the industrial development in the Lianyun EDZ such as sewage treatment, property leasing and inland port handling, which help facilitate enterprises to move in their production lines and reduce the cost of conducting businesses in the Lianyun EDZ.

Yungang Group’s policy role is expected to be maintained as the key developer in the Lianyun EDZ and SCO Park in the next 12-18 months. Its businesses will increase along with the development of the SCO Park and Lianyun EDZ, including the construction of supporting facilities and provision of services. Given Yungang Group’s essential roles, the replacement cost for the local government is high and the ongoing government support is very likely.

Medium exposure to commercial activities

Yungang Group maintained medium exposure to commercial business, which has increased along with the rising local industrial investments. The Company is engaged in commercial activities including trading, services, PV power generation and property leasing, which generate additional income sources. The risk nature of such activities is generally higher than traditional infrastructure construction projects and direct government financial support will be more difficult under stricter regulatory supervision on the increase in government's implicit debt. Yungang Group relies on external financing to support the development of its commercial activities.

In order to support local industrial development, Yungang Group provides industrial sewage treatment and inland port handling services to local enterprises, which are self-sustaining businesses. The Company is the only industrial sewage service provider in the park and has strong regional advantages. As of 30 June 2024, the Company owned and operated 1 sewage treatment plant with a total treatment capacity of 350 million tons per day, covering a sewage service area of approximately 10 square kilometers. At the same time, the Company had a sewage treatment project under construction with a total investment of RMB800.0 million and an uninvested amount of RMB583.0 million. However, with its policy-driven nature, the pricing flexibility is low, making Yungang Group less resilient to changes in operating costs. In addition, due to the renovation expenses for upgrading the ports, the Company continued to experience negative profit margins in its port handling business in 2023. The performance of the port handling business fluctuates by regional logistic flow.

Yungang Group is also engaged in trading business to meet the needs of local enterprises. The product scope has shifted quickly in recent years. In 2023, the main trading goods were rebar, coiled screw, and agricultural products such as soybean. The trading business represents a large portion of its revenue stream but generates a minimal profit. Yungang Group's trading business has low price risk as most orders are fulfilled on an on-demand basis. However, the suppliers and customers of the trading business were still highly concentrated. There are also some additional capital needs for trading business because a credit period of no more than 30 days is normally provided to customers.

Yungang Group also carried out self-operated projects. As of 30 June 2024, the Company mainly had 3 self-operated projects under construction, including an industrial park, a grain storage project and a cold chain warehouse project, with a total investment of RMB1.3 billion and an uninvested balance of RMB1.0 billion. The Company mainly relies on leasing to achieve fund balancing. However, the initial project capital investment brings certain expenditure pressure to the Company.

Yungang Group started its PV power generation business through the acquisition of two enterprises with PV power installed capacity of 16MW in 2019. The PV power generation has offered a stable recurring income source to the Company, with high gross profit margin. In 2023, the revenue from PV power generation slightly increased to RMB15.0 million from RMB14.0 million last year.

Track record of receiving government support

Yungang Group has a track record of receiving government support in various forms such as capital injection, financial subsidies, as well as equity and asset injections. For instance, in the first half of 2024, the local government transferred its holding and assets of three grain-related state-owned enterprises to the Company without compensation, increasing its capital reserves. In order to support the Company's operation, the local government has also provided ongoing financial subsidies of RMB112.3 million in total from 2023 to 2024H1.

Besides, the Company also receives government support in the form of project allocation and assistance in the application of special bond funds. The Company will undertake more important tasks along with the development of Lianyun EDZ and SCO Park. For example, the Company is engaged in the investment of tidal flat solar photovoltaic power generation project, an important project of Lianyungang Municipal Government. Given the Company's strong public policy role in the Lianyun EDZ and the SCO Park, we expect the Company will continue to receive government support over the next 12 to 18 months.

Rising debt level driven by expanding local investments

Yungang Group demonstrated ongoing debt growth driven by continuous investment in projects. The Company's total debt increased to RMB6.9 billion at mid-2024 from RMB5.2 billion at end-2023. Its total capitalization ratio remained at a moderate level and increased from 52.0% to 58.9% during the same period. Yungang Group has a large investment plan for its infrastructure construction and commercial activities. As of 30 June 2024, all the projects under construction and planning require an outstanding investment of RMB2.3 billion. Although some of them can be supported by government special funds, there are still large external financing needs for construction projects. The Company's debt level is expected to increase in the next 12 to 18 months along with ongoing investment.

Moderate access to funding with limited financing flexibility

Yungang Group has moderate access to funding. It relies highly on indirect financing and has limited access to the domestic debt market. The reliance on asset-pledged loans improved as deeper cooperation with banks. In addition, the Company still maintained a high reliance on short-term debt, which accounted for 77.0% of total debt as of 30 June 2024. At the same time, approximately 39.1% of Yungang Group's assets were restricted as collaterals for financing, which limits its financing flexibility. The limited access to funding will also make Yungang Group less resilient to the change in the financing market environment. In addition, the Company's exposure to non-standard financing accounted for less than 10% of total debts as of 30 June 2024.

The Company has relatively weak balance-sheet liquidity and requires refinancing for its operations. As of 30 June 2024, the Company had cash on hand of RMB3.8 billion, which was insufficient to cover its short-term debts of RMB6.9 billion. Yungang Group maintained a good relationship with domestic banks. Its credit line has increased compared with last year, but stand-by facilities were small. As of 30 June 2024, the Company had total credit facilities of RMB4.4 billion and undrawn credit facilities of RMB178.3 million.

Large exposure to external guarantees provided to local state-owned enterprises

Yungang Group has a large exposure to contingent liabilities from its external guarantees provided to external parties. As of the end of June 2024, its external guarantees increased to RMB3.3 billion from RMB2.9 billion as of the end of June 2023, accounting for 68.9% of its net assets. All of these external guarantees were provided to other local LIIFCs or state-owned enterprises. For example, the Company provided external guarantees of RMB707.3 million to HZDG, a subsidiary of Haizhou Bay Holding. In case a credit event occurs, the Company may face certain contingent liability risks and cross-default risks, which are negative to its credit quality.

ESG Considerations

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

The Company is also exposed to social risks as a public services provider in Lianyun District, Lianyungang City. Demographic changes, public awareness, and social priorities shape the government's target for Yungang Group or affect the government's propensity to support the Company.

Yungang Group's governance considerations are also material as the Company is subject to oversight and reporting requirements to 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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