

Credit Opinion

18 December 2024

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

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Dongying District Municipal Holding Group Co., Ltd.

Surveillance credit rating report

CCXAP affirms Dongying District Municipal Holding Group Co., Ltd.'s long-term credit rating at BBB_g-, with stable outlook.

Summary

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

Our assessment of Dongying District Government's capacity to provide support reflects Dongying District's moderate economic strength and fiscal metrics.

The rating also reflects the local government's willingness to provide support, based on the Company's (1) important role in local infrastructure construction and public services; and (2) good track record of receiving government support.

However, the rating is constrained by the Company's (1) increasing debt burden driven by the continuous investment in construction projects; (2) weak liquidity profile with limited bank standby facilities; and (3) medium contingent liabilities risk caused by mutual guarantee for local state-owned enterprises ("SOEs").

The stable outlook on DYM's rating reflects our expectation that the local government's capacity to provide support will remain stable, and the Company's characteristics such as its important role in the infrastructure construction and public services of Dongying District will remain unchanged over the next 12-18 months.

Rating Drivers

- Important role in local infrastructure construction
- High sustainability in provision of public services
- Good track record of receiving government support
- Increasing debt burden driven by the continuous investment in construction projects
- Weak liquidity profile with limited bank standby facilities
- Medium contingent liabilities risk caused by mutual guarantee for local SOEs

Rating Sensitivities

What could upgrade the rating?

The rating could be upgraded if (1) the Dongying District Government's capacity to support strengthens; and (2) the Company's characteristics change in a way that enhances the local government's willingness to support, such as improved financing ability.

What could downgrade the rating?

The rating could be downgraded if (1) the Dongying District 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 reduced strategic significance, deteriorated financing ability, or decreased government payments.

Key Indicators

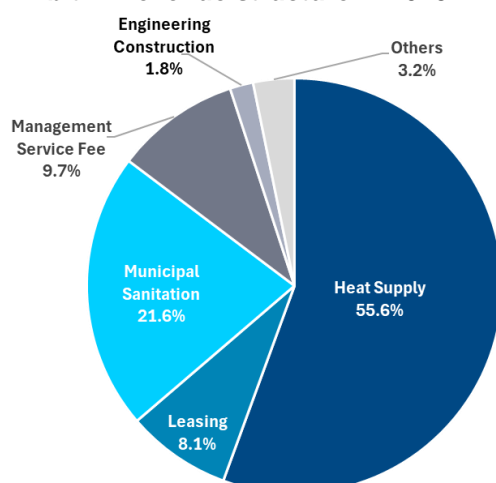
	2021FY	2022FY	2023FY	2024H1
Total Asset (RMB billion)	10.1	11.3	10.6	12.2
Total Equity (RMB billion)	5.5	5.7	5.7	5.7
Total Revenue (RMB billion)	0.7	0.7	0.8	0.4
Total Debt/Total Capital (%)	29.5	36.1	35.8	41.6

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

Source: Company data, CCXAP research

Corporate Profile

Founded in 2018, DYMH is one of the key local infrastructure investment and financing companies ("LIIFCs") in Dongying District. The Company shoulders the major responsibility of carrying out local public activities, including infrastructure construction, heat supply, and municipal sanitation. It also engages in commercial activities such as self-operated project construction and leasing. As of 30 June 2024, DYMH was wholly owned and controlled by the State-owned Assets Management Service Center of Dongying District, Dongying City.

Exhibit 1. Revenue structure in 2023

Source: Company information, CCXAP research

Rating Considerations

Government's Capacity to Provide Support

We believe Dongying District Government has a relatively strong capacity to provide support given its moderate economic strength and fiscal metrics.

Shandong is the third largest province in China by gross regional products ("GRP"), with a solid foundation in different industries such as logistics, shipbuilding, marine technology, chemical, automotive, and agri-food. Dongying City is a prefecture-level city located in the northeast part of Shandong Province. Dongying City owns rich oil and gas resources, 80% of Shengli Oilfield's oil geological reserves and 85% of production are concentrated in Dongying City. The petrochemical industry is the most important pillar industry in Dongying City. After industrial transformation and upgrading, Dongying City has also developed some emerging industries including new energy and new materials, high-end chemical industry, as well as high-end equipment.

In 2023, Dongying City recorded a GRP of RMB389.9 billion, recording an economic growth of 7.0% year-over-year ("YoY") and ranking 9th among 16 prefecture-level cities in Shandong Province. Dongying City has relatively strong fiscal strength and moderate fiscal balance. In 2023, Dongying City's general budgetary revenue was RMB28.5 billion, and tax revenue accounted for 70.2% of the general budgetary revenue. Its average general budgetary revenue to general budgetary expenditure ratio was 77.8% over the past three years. As of 31 December 2023, Dongying City Government reported an outstanding government debt of RMB90.5 billion and accounted for 23.2% of its GRP. In the first three quarters of 2024, Dongying City reported a GRP of RMB313.1 billion, representing 6.5% YoY growth.

Exhibit 2. Key economic and fiscal indicators of Dongying City

	2021FY	2022FY	2023FY
GRP (RMB billion)	344.1	362.1	389.9
GRP Growth (%)	8.5	4.3	7.0
General Budgetary Revenue (RMB billion)	26.2	26.5	28.5
General Budgetary Expenditure (RMB billion)	30.1	36.9	38.2
Local Government Debt (RMB billion)	61.6	74.5	90.5

Source: Dongying Municipal Government, CCXAP research

Dongying District is the central district of Dongying City. Supported by rich oil and gas resources, Dongying District has mainly developed fine chemical and petroleum supporting industries. Shengli Oilfield's base, the second largest oil field in China, located in Dongying District. Dongying District is also the largest petroleum equipment industry base and petroleum equipment product export base in China. In 2023, Dongying District reported a GRP of RMB59.2 billion, recording an economic growth of 6.3% YoY. However, its general budgetary revenue has continued to decline in the past three years, falling from RMB4.1 billion in 2021 to RMB3.5 billion in 2023. During the same time, its general budgetary revenue to general budgetary expenditure ratio also decreased from 106.4% in 2021 to 63.4% in 2023. Moreover, Dongying District relies on the transfer income to balance its excess government fund expenditure. The average transfer income of Dongying District was RMB3.6 billion over the past three years. As of 31 December 2023, Dongying District Government reported an outstanding government debt of RMB9.5 billion and accounted for 16.0% of its GRP.

Exhibit 3. Key economic and fiscal indicators of Dongying District

	2020FY	2021FY	2023FY
GRP (RMB billion)	53.1	56.7	56.7
GRP Growth (%)	11.8	5.4	5.4
General Budgetary Revenue (RMB billion)	4.1	3.9	3.9
General Budgetary Expenditure (RMB billion)	3.9	5.1	5.1
Local Government Debt (RMB billion)	4.3	6.9	6.9

Source: Dongying District Government, CCXAP research

Government's Willingness to Provide Support

Important role in local infrastructure construction

There are 3 major LIIFCs in Dongying District under the control of Dongying District Government. Each of them has a clear position under the government's planning. Among them, DYM is the key entity in infrastructure construction and provision of public services in Dongying District, mainly responsible for heat supply, renovation of old urban residential communities, road construction and improvement, river management, and municipal sanitation.

DYM carries out various infrastructure construction projects mainly through self-construction model. Under self-construction model, the Company is responsible for the fund raising of the projects and achieves fund balancing from revenue in other commercial projects. However, the revenue from commercial projects has more uncertainties than direct government payment, which may bring larger financial repayment pressure to the Company under self-construction model. As 30 June 2024, there were 5 main projects under construction, with a total investment of RMB1.5 billion and uninvested amount of RMB145.0 million, mainly including rehabilitation of old areas and construction of schools. DYM is also engaged in infrastructure construction business through engineering construction projects, with Class III qualification for general contracting of municipal utility engineering, professional contracting of urban and street lighting engineering and professional contracting of environmental protection engineering. The Company has completed several infrastructure construction projects as at 30 June 2024. However, the volume of engineering construction business has been limited, with the total order amount of RMB332.2 million as of 30 June 2024.

High sustainability in provision of public services

DYM is the regional dominant heat supplier in urban district of Dongying District by providing heat energy to residential and commercial customers with pipe network length of around 307 kilometers, serving around 212.4

thousand residential users and 7.9 thousand non-resident users as of end-2023. However, given the public utility nature of heat supply, the Company's heat supply business aims to assure local people's livelihood and charges at a price lower than cost, resulting operating loss in recent years.

Moreover, DYMH is in charge of the municipal sanitation business with municipal utility operating license, including environmental sanitation and cleaning, garbage classification, property services, greening maintenance, garbage collection and transportation and smart parking, with a total road cleaning area of approximately 14.5 million square meters. The revenue from this business increased from RMB132.1 million in 2022 to RMB173.5 million in 2023.

Considering the indispensability and high sustainability of these public services, we believe the replacement cost of the Company is high.

Good track record of receiving government support

DYMH has a good track record of receiving support from Dongying District Government in terms of subsidies, capital injection, special funds, and equity transfer. From 2021 to 2023, the local government consistently provided subsidies for the Company, mainly supporting its heat supply services. In 2022, the local government allocated funds of RMB507 million to DYMH as its shareholder, which enhanced its capital strength. Given the Company's important role in Dongying District, we believe that DYMH will continue to receive various kinds of support from the local government.

Increasing exposure to commercial activities

Apart from the public policy activities, DYMH also engages in commercial activities such as leasing. Given that the proportion of commercial assets to total assets was less than 30%, we estimate the DYMH's exposure to commercial activities is low. However, the risk exposure increased from the previous year due to the increase in the construction of self-operated projects.

The Company's main leasable assets are rainwater and sewage pipe network and properties. DYMH signed a pipe network leasing contract with the Dongying District Comprehensive Administrative Law Enforcement Bureau, with an annual rent of RMB56 million and 10-year leasing period starting at 2019. This part of the rent is settled on an annual basis with a timely repayment. The main leasable property assets are the Administrative Approval Hall, Huatai International Financial Center, stadium and parking lots. Administrative Approval Hall and Huatai International Financial Center are self-purchased properties, while other leasable assets are transferred by local government. The leasing business could provide certain supplementary revenue to the Company. In 2023, the revenue from leasing business was RMB65.5 million, accounting for 8.1% of its total revenue. The major lessees are government related departments. However, some rents are in arrears without clear payment schedule and the rental repayment for the Administrative Approval Hall is lagging. We believe that the risk caused by leasing business is controllable as most of leasable assets are transferred by the local government.

In addition, the Company participates in self-operated commercial projects construction in Dongying District to promote local urban development. However, the revenue from commercial projects is heavily influenced by the local economic conditions. As of 30 June 2024, there were 2 main self-operated commercial projects under construction, with a total investment of RMB6.1 billion. These projects are hospital and cultural tourism projects. The uninvested amount of these self-construction commercial projects was around RMB4.9 billion as of mid-2024, which would cause certain capital expenditure pressure for the Company.

Increasing debt burden driven by the continuous investment in construction projects

DYMH's total debt increased from RMB2.3 billion at end-2021 to RMB4.1 billion at mid-2024, due to the continuous investment in construction projects in Dongying District. Meanwhile, DYMH's capitalization ratio increased from 29.5% to 41.6%. As of 30 June 2024, the Company's short-term debt was RMB1.1 billion and its short-term debt to total debt ratio was 26.7%, indicating certain refinancing pressure. As of 30 June 2024, there were 8 main projects under construction and planning, with a total investment amount of approximately RMB7.6 billion and uninvested amount of RMB5.0 billion. Given the large uninvested amount of construction projects and maturing debt, we estimate the Company would continue to rely on external financing such as bank loans and its total debt would further increase over the next 12-18 months.

Weak liquidity profile with limited bank standby facilities

DYMH's access to funding is fair. Bank loans accounts for the majority of the Company's total debt. The Company shows low standby liquidity. As of 30 June 2024, the Company had obtained total bank facilities of RMB3.0 billion, but the available bank facilities were only RMB6.8 million. Moreover, the Company's bank loans were concentrated on regional banks, such as Dongying Bank. Loans from Dongying Bank accounted for around 40.6% of total bank loans, which may bring higher financing costs and uncertainties in future refinancing due to the concentration on regional banks. In addition to regional banks, DYMH has also established long-term borrowing relationship with policy banks and large domestic banks such as Industrial and Commercial Bank of China Limited and Agricultural Development Bank of China. The Company also issued two tranches of offshore bonds in 2024, raising a total amount of RMB1.1 billion, with coupon rates of 4.6% and 6.8% respectively. The Company's exposure to non-standard financing is low, and financing leasing accounted for less than 10% of total debt.

Meanwhile, the liquidity of the Company's assets was relatively weak. As of 30 June 2024, inventories, other receivables, and fixed asset accounted for approximately 75% of total assets. The inventories are mainly cost of infrastructure construction and self-construction projects, while the fixed assets are mainly pipeline network assets, which are considered low liquidity. In addition, the total restricted assets were RMB2.5 billion which accounted for 20.9% of total assets, and heating pipeline network was the largest component. The low asset liquidity may undermine the Company's financial flexibility.

Medium contingent liability risk caused by mutual guarantee for local SOEs

DYMH bears moderate contingent risk resulting from large external guarantees. As of 30 June 2024, the Company's external guarantees amounted to RMB3.8 billion, accounting for 67.8% of its net assets. Most of the external guarantees were provided to SOEs. There is only one guaranteed company which is a private-owned enterprise, and the Company holds a minority shareholding in this company. Meanwhile, 89.7% of its external guarantees was provided to Dongying District Urban Development Investment Group Co., Ltd ("DYUD"), which is one of the most important LIIFCs in Dongying District. The guarantee is primarily due to DYUD undertaking the urban renewal project in Dongying District, which requires a large scale of bank loans. The practice of mutual guarantees among local SOEs is common phenomenon in Dongying District. In case a credit event occurs, the Company may face certain contingent liability risks and cross-default risks. Considering the important role of state-owned enterprises in Dongying District, we expect that the local government would provide support when necessary.

ESG Considerations

DYMH is exposed to environmental risks due to undertaking key infrastructure construction. Such risks could be moderated by conducting environmental studies and planning prior to the start of the projects, and close monitoring during the construction phase.

The Company bears social risks as it implements public policy initiatives by playing an important role in the social welfare of Dongying District. 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.

DYMH's governance considerations are also material as the Company is subject to oversight by Dongying District 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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