

Credit Opinion

25 February 2025

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

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Heze Finance Investment Group Co., Ltd.

Surveillance credit rating report

CCXAP affirms Heze Finance Investment Group Co., Ltd.'s long-term credit rating at BBB_g+, with stable outlook.

Summary

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

Our assessment of Heze Municipal Government's capacity to provide support reflects Heze City's increasing economic strength and moderate fiscal metrics.

The rating also reflects the local government's very high willingness to provide support, based on the Company's (1) strategic role in investing and constructing key municipal projects and the economic and social development of Heze City; and (2) good track record of receiving government supports.

However, the rating is constrained by the Company's (1) high exposure to commercial activities; and (2) medium contingent risks resulting from external guarantees.

The stable outlook on HZFI's rating reflects our expectation that the local government's capacity to provide support will remain stable, and the Company will maintain its strategic role in the economic and social development of Heze City over the next 12-18 months.

Rating Drivers

- Strategic role in investing and constructing key municipal projects and the economic and social development of Heze City
- Providing public services with regional dominance
- Good track record of receiving government supports
- High exposure to commercial activities
- Increasing debt burden driven by ongoing investments in construction projects
- Access to different funding channels
- Medium contingent risks resulting from external guarantees

Rating Sensitivities

What could upgrade the rating?

The rating could be upgraded if (1) Heze Municipal 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 lower exposure to risky commercial activities and improved financing ability.

What could downgrade the rating?

The rating could be downgraded if (1) Heze 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 support, such as reduced strategic significance, decreased government payments, or deteriorated debt management.

Key Indicators

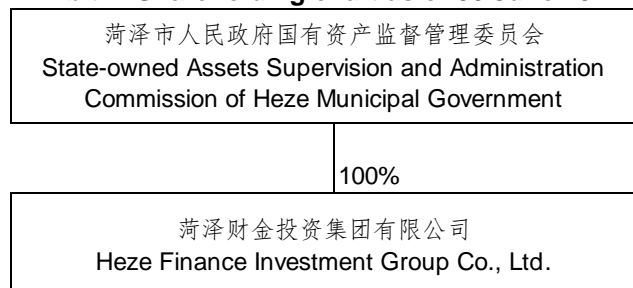
	2021FY	2022FY	2023FY	2024H1
Total Assets (RMB billion)	30.3	32.4	36.7	37.0
Total Equity (RMB billion)	14.6	14.7	15.1	15.1
Total Revenue (RMB billion)	5.2	5.4	5.8	2.3
Total Debt/Total Capital (%)	28.6	33.4	41.3	43.2

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

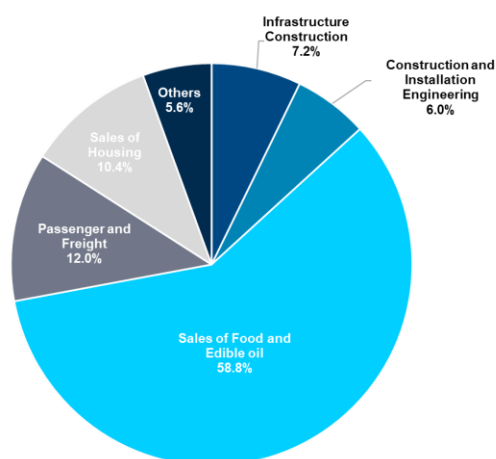
Source: Company data, CCXAP research

Corporate Profile

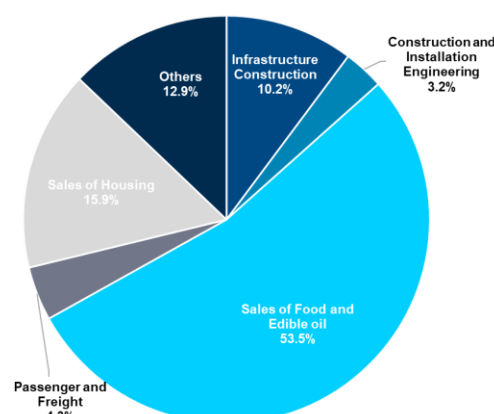
Founded in March 1994, HZFI is an important local infrastructure investment and financing company ("LIIFC") in Heze City, which is one of the leading entities in the development blueprint of Heze Municipal Government. The Company plays a strong strategic role in the social, economic, and urban development of Heze City. Specifically, HZFI is responsible for major public policy projects, including infrastructure construction, land development and consolidation, policy-oriented grain storage, and public transportation. It also engages in commercial activities such as sales of housing, sales of commercial food and edible oil, cultural tourism, as well as industrial investment. As of 30 June 2024, the State-owned Assets Supervision and Administration Commission of Heze Municipal Government ("Heze SASAC") had 100% ownership of HZFI.

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

Exhibit 3. Gross profit structure in 2023**Rating Considerations****Government's Capacity to Provide Support**

We believe the local government of Heze City has a very strong capacity to provide support given its sound economic fundamentals, with increasing economic strength and moderate 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. Heze City is a prefecture-level city of Shandong Province and is located in the southwest of Shandong Province with a good economic foundation. Heze City's GRP ranked 8th among 16 prefecture-level cities in Shandong Province over the past three years. Heze City's economic growth is mainly driven by the key industries including the high-end chemical industry, biomedicine, mechanical and electrical equipment manufacturing, new energy and new material, agricultural and sideline products, as well as trade logistics and e-commerce.

In 2023, Heze City reported a GRP of RMB446.4 billion, recoding an economic growth of 6.8% year-over-year ("YoY"). According to the preliminary result, Heze City's GRP amounted to RMB480.3 billion in 2024, representing a YoY increase of 6.1%. Heze City demonstrated improving comprehensive strength over the past three years. The general budgetary revenue of Heze Municipal Government also increased from RMB28.4 billion in 2021 to RMB31.7 billion in 2023. Its fiscal balance was modest, with a general budgetary revenue to general budgetary expenditure ratio of 43.1%, and tax accounted for 64.8% of the general budgetary revenue in 2023. The Heze Municipal Government continues to receive large number of transfer payment from the Shandong Province, demonstrating its importance in Shandong Province. From 2021 to 2023, Heze Municipal

Government totally received the transfer payments of RMB118.0 billion from Shandong Provincial Government. However, the government fund income dropped by 11.2% YoY to RMB36.0 billion in 2023 due to the reduction of state-owned land use rights transfer. This income is mainly affected by regulatory policies and the land market, we expect the downturn of the real estate industry may weigh on the land sales in following years. As of 31 December 2023, Heze Municipal Government reported an outstanding government debt of RMB150.1 billion and accounted for 33.6% of its GRP, increasing from that of RMB131.2 billion and 31.2% as of 31 December 2022.

Exhibit 4. Key economic and fiscal indicators of Heze City

	2021FY	2022FY	2023FY
GRP (RMB billion)	397.7	420.5	446.4
GRP Growth (%)	8.8	4.2	6.8
General Budgetary Revenue (RMB billion)	28.4	30.1	31.7
General Budgetary Expenditure (RMB billion)	63.3	69.2	73.5
Local Government Debt (RMB billion)	110.8	131.2	150.1

Source: Heze Municipal Government, CCXAP research

Government's Willingness to Provide Support

Strategic role in investing and constructing key municipal projects and the economic and social development of Heze City

HZFI is one of the most important LIIFCs in Heze City that undertakes city development projects and provision of public services. It is also positioned as a pivotal entity in state-owned capital operation in Heze City. HZFI focuses on the key infrastructure construction projects, policy-oriented grain storage, public transportation, as well as land development and consolidation, which are crucial to the economic and social development of Heze City. The Company has performed well in undertaking major livelihood projects in Heze City.

HZFI carries out key infrastructure construction projects on both agent construction basis and self-construction basis. Under agent construction basis, the Company signs an entrusted construction contract with the entrusting unit (mainly government departments and local state-owned enterprises) in relation to its infrastructure construction services and is in charge of the implementation of certain major public infrastructure projects. As of 30 June 2024, HZFI had completed several projects consisting of pipeline of heating supply, hospital, government service center, as well as school. At the same time, the Company had a total of 9 projects under construction, with a total investment of RMB1.4 billion and an outstanding amount of RMB543.0 million, which are mainly rural revitalization projects, parks and so on. These projects are essential to local economic development and provide benefits to the public and local employment.

According to business plan of HZFI, the Company would gradually switch the business model of infrastructure construction from agent construction basis to self-construction basis. There were 2 key self-construction projects under construction, namely, Heze Municipal Hospital East Campus and Water Storage & Supply Security Project, with a total investment of RMB4.0 billion and an outstanding amount of RMB3.0 billion. Heze Municipal Hospital East Campus is the important livelihood project in Heze City and is expected to be the largest medical complex in Southwest Shandong Province after completion. Water Storage & Supply Security Project is the key water conservancy project aimed at alleviating local water shortages and enhancing water supply security in Heze City. These two projects also receive government special fund to support its construction, which would partially mitigate the Company's capital expenditure pressure.

HZFI also engages in municipal project construction through engineering construction model, with relevant construction qualifications. The Company acquires projects through open market or negotiation with third parties, which are mainly concentrated in Heze City. Thanks to its strategic position in regional development, the Company has certain advantages in acquiring local municipal projects with multiple contracts in hand. From 2023 to the first half of 2024, the Company newly signed 10 engineering construction projects totaling approximately RMB201.0 million. However, the Company's operating subsidiary is listed as a dishonest judgment debtor several times from 2021 to 2025, mainly owing to the Company's qualifications being borrowed. The Company plans to resolve these dispute cases by the first half of 2025. Moreover, the Company intends to focus on internal business and gradually reduce external market-based business in the future in order to reduce business risks.

In addition, HZFI participates in the land development and consolidation business in rural land remediation projects in Heze City, by conducting works on homesteads within the pilot areas. The Company is required to invest funds and entrust enterprises to dismantle, reorganize and reclaim rural construction land into cultivated land to create surplus land quotas, that are exchanged in Shandong Province. As of 30 June 2024, the Company had 2 lands to be consolidated, with a total area of 4.9 million square meters and an estimated investment amount of around RMB145.7 million. However, the Company did not recognize any income in 2023 and the first half of 2024, which is mainly due to the fact that no land transfer transactions have been generated in recent years.

Providing public services with regional dominance

HZFI is responsible for policy-oriented grain storage involving the purchase, storage, transfer, and wholesale of grain and edible oil. The main products are municipal-level grain reserves, national grain with minimum purchase prices, and national temporary grain reserves, respectively, that guarantee food supply in the society. The local government also provides subsidies to the business due to its public welfare nature. As of 30 June 2024, the Company had total reserves of 170.0 thousand tons of municipal-level grain, 140.0 thousand tons of national grain with minimum purchase prices, and 34.0 thousand tons of national temporary grain. Moreover, the Company owned 35 grain storage areas in Heze City and total capacity of 1.5 million tons.

Meanwhile, HZFI is the leading public transport operator, providing transport services within the majority area of Heze City, including the road passenger transport, urban public transport, school bus transport, taxi and vehicle leasing. The Company takes part in this dominant business in terms of contracting and self-operating various public vehicles, mainly operating long-distance passenger transport between urban areas (counties) to other urban areas, intercity buses from Heze City to various counties, urban and rural public transport, as well as public transport within several counties, including Juancheng, Chengwu, and Shanxian. As of 30 June 2024, HZFI had over 2,000 public vehicles operating in 185 routes, with the amount of annual transported passengers reaches approximately 13 million.

Overall, we believe that the replacement cost of the Company is high as these public services are essential for local residents, showing high sustainability.

Good track record of receiving government supports

HZFI has a good track record of receiving support from the local government in terms of subsidies, capital injection, special funds, and equity transfers. Since its establishment, HZFI has received cash and asset injections such as equity shares and buildings from the local government, which has greatly improved its capital strength and increased operating assets. For instance, the Company's capital reserves increased by RMB234.0

million in 2023, mainly due to the cash injection from local government. In addition, from 2023 to 2024H1, the Company received ongoing subsidies for carrying out policy-support activities such as infrastructure construction projects and policy-oriented grain storage business, with total amount of approximately RMB424.8 million. At the same time, the local government provided special bond of RMB412.0 million to support the Company's ongoing construction and operation.

Considering HZFI's strategic role in Heze City and close relationship with Heze Municipal Government, we expect the local government will continue to enlarge the Company's asset size through cash and asset injection. We also believe that the Company will receive subsidies and special bonds from the local government in a timely manner.

High exposure to commercial activities

HZFI engages in various commercial activities mainly including sales of housing, sales of commercial food and edible oil, cultural tourism, as well as industrial investment. HZFI's commercial assets accounted for large proportion of total assets in our estimation, some of the commercial activities are subject to volatile market and counterparties risk.

Sales of food and edible oil is the main business of HZFI, which covers more than 290 prefecture-level cities and contributed most the Company's revenue over the past 3 years. The Company adopts both direct selling and agent selling models. The Company's top 5 customers accounted for 6.1% of total sales in 2023, showing a low concentration. Moreover, around 80% of business was settled by cash or prepaid payment, therefore, we believe the risk associated with this business is controllable.

In addition, HZFI has engaged in housing sales within Heze City, mainly commercial residential housings that highly concentrated in Heze City. As of 30 June 2024, most of the completed commercial housings were sold, with a high selling rate of 96.7%. However, the number of uninvested projects poses large capital expenditure pressure to the Company, which will be relied on external financing. As of 30 June 2024, HZFI had 3 projects under construction, with a total investment of RMB5.4 billion and an uninvested amount of RMB1.7 billion. During the downturn in China's property market, the fund balancing would experience high volatility, causing higher business and financial risks to the Company.

According to the strategic plan of HZFI, the Company would carry out self-operation projects, including industrial projects and cultural tourism projects. The Company has operated two tourism projects, including Chinese Peony Garden and Caozhou Peony Garden, and generated income from the sales of ticket, commodity sales of related peony industries, hosting business events and study tour. Meanwhile, the Company has a Fangte Fantasyland project under construction with an estimated total investment of RMB1.1 billion and an outstanding amount of RMB664.0 million. Upon completion, the Company plans to recover the cost from operating income. Moreover, the Company has 2 projects under planning, which are Heze Shengyu Cold Chain Logistics Project and vocational school, with an estimated investment amount of RMB1.6 billion. The Company plans to achieve fund balancing through operating revenue such as leasing and selling income. The large investment amount of self-operation projects may further enlarge the Company's capital expenditure pressure. Considering the importance of these projects to the economic and industrial development of Heze City, the Company is expected to receive funding from special bonds supported by the local government for some self-operated projects, which could partially relieve its capital expenditure pressure.

Furthermore, HZFI conducts industrial investment business through fund investment, equity investment, and debt investment to support local industries, in relation to its assigned role as an industrial investment entity. The

industries that the Company primarily invests in are also in line with the local pillars industries, such as biomedicine, mechanical and electrical equipment manufacturing, as well as new energy. However, the returns of these investments are subject to the operation risk and financial performance of the investees, in our view.

Increasing debt burden driven by ongoing investments in construction projects

With the continuous financing for construction projects, HZFI shows fast debt growth. As of 30 June 2024, the Company's total debt increased to RMB11.5 billion from RMB7.4 billion as of end-2022, while its total capitalization ratio increased to 43.2% from 33.4% during the same period. Meanwhile, HZFI still demonstrated certain short-term debt pressure but gradually improved its debt structure. The Company's short-term debt remained a relatively large proportion of total debt, accounting for 36.8% as of 30 June 2024, decreasing from 43.2% at the end of 2022. At the same time, the cash to short-term debt ratio maintained at around 0.7x at mid-2024, indicating that its cash balance could not fully cover its short-term debt. We expect that the Company will continue to rely on external financing such as bank loans and its debt burden would increase, considering ongoing investment in projects under construction in the next 12-18 months.

HZFI maintained moderate asset liquidity. As of 30 June 2024, the Company's inventories, receivables account, fixed assets, and other non-current assets accounted for 67.0% of the total assets. The inventories mainly consist of construction development costs, while receivables mainly consist of transactions with the government and other state-owned enterprises. Other non-current assets mainly include the Chinese Peony Garden and Caozhou Peony Garden, which could generate supplementary cashflow to the Company. In addition, the Company pledged a number of assets for loans, mainly fixed assets and construction in progress, accounting for 11.2% of total assets as of 30 June 2024.

Access to different funding channels

The Company has access to different funding channels, such as bank loans, bond market, and non-standard financing. Bank loans contribute the most of its total debts, which accounted for more than 60.0% of the total debt as of 30 June 2024. The Company has built long-term relationships with various domestic banks in China, including Agricultural Development Bank of China, China Construction Bank Corporation, and Heze Rural Commercial Bank Co., Ltd. As of 30 June 2024, the Company received total credit facilities of RMB8.8 billion and the available portion being RMB1.1 billion.

The Company also has a track record for fund-raising activities in the debt capital market, including onshore and offshore debt markets. From 2023 to 2024, the Company has raised RMB3.0 billion through 4 tranches of private bonds, with the coupon rates from 2.4% to 5.37%. Moreover, the Company tapped into the offshore debt market in 2024. The Company issued a tranche of 3-year offshore bond, raising RMB485.0 million, with a coupon rate of 3.2%. In addition, the Company's exposure to non-standard products (mainly financial leasing) decreased, accounting for around 15% of the total debts as of 30 June 2024. In view of the HZFI's important status and key role in the social and economic development of Heze City, we expect the Company would maintain stable funding access from its diversified funding channels.

Medium contingent risks resulting from external guarantees

HZFI maintained a moderate exposure to external guarantees. As of 30 June 2024, the external guarantee amount of HZFI was RMB2.7 billion, accounting for 17.6% of its net asset. The Company has reduced the external guarantees to privately-owned enterprises, and all existing external guarantees were provided to other

state-owned enterprises in Heze City. However, in case a credit event occurs, the Company may face certain contingent liability risks.

ESG Considerations

HZFI is exposed to environmental risks due to undertaking infrastructure construction and land consolidation. Such risks could be mitigated by conducting environmental studies and detailed planning prior to the start of the projects and close monitoring during the construction phase. HZFI's key operations are in material compliance with currently applicable national and local environmental, health and safety laws and regulations.

In terms of social awareness, the Company has played a crucial role in the social welfare of Heze City by undertaking policy-oriented grain storage and public transportation services. Demographic changes, public awareness and social priorities shape the government's development strategy, and it will affect the government's propensity to support the Company.

HZFI's governance considerations are also material as the Company is subject to oversight by Heze 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 \(July 2022\)](#).

Appendix

Exhibit 5. Peer Comparison

	Heze Finance Investment Group Co., Ltd.	Heze Investment Development Group Co., Ltd.	Heze Urban Construction Engineering Development Group Co., Ltd.
Long-Term Credit Rating	BBB _g +	BBB _g +	BBB _g +
Shareholder	Heze SASAC (100%)	Heze SASAC (97.93%) and Shandong Caixin Asset Operation Co., Ltd. (2.07%)	Heze Investment Development Group Co., Ltd. (50.4%) and Heze City Investment Holdings Group Co., Ltd. (49.6%)
Positioning	Pivotal entity in state-owned capital operation and key municipal project investment and financing platform of Heze City	Pivotal entity in state-owned capital operation and key municipal industry investment and financing platform of Heze City	Major entity in infrastructure construction and public services in Heze City
Total Assets (RMB billion)	36.7	67.1	26.7
Total Equity (RMB billion)	15.1	34.0	9.4
Total Revenue (RMB billion)	5.8	8.4	4.2
Total Debt/Total Capital (%)	41.3	35.2	46.7

All ratios and figures are calculated using CCXAP's adjustments based on financial data as of 31 December 2023.

Source: Company data, CCXAP research

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