CCXAP assigns first-time long-term credit rating of BBB_g- to Shandong Zhicheng Agricultural Development Group Co., Ltd., with stable outlook.

Hong Kong, 22 May 2024 – China Chengxin (Asia Pacific) Credit Ratings Company Limited (“CCXAP”) has assigned first-time long-term credit rating of BBBg- to Shandong Zhicheng Agricultural Development Group Co., Ltd. (“SDZC” or the “Company”), with stable outlook.

The BBB_g- long-term credit rating of SDZC reflects Zoucheng City Government’s (1) strong capacity to provide support; and (2) 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 Zoucheng City’s relatively good economic strength and fiscal metrics, ranking it among the Top 100 counties in China and as the top county in Jining City by gross regional production (“GRP”).

The rating also reflects the local government’s willingness to support, which is based on the Company’s (1) status as the sole state-owned enterprise (“SOE”) focusing on agricultural development in Zoucheng City; and (2) good track record of receiving government support. However, the rating is constrained by the Company’s (1) increasing exposure to commercial activities with relatively large investment needs; (2) fast debt growth with relatively large short-term debt burden; and (3) fair access to funding with high reliance on urban commercial banks.

Corporate Profile

Established in January 2018, SDZC is one of the key SOEs in Zoucheng City and focuses on agricultural development in Zoucheng City. In accordance with the economic and industrial development plan of Zoucheng City, SDZC is responsible for rural revitalization and agricultural development by undertaking policy-driven projects, including land consolidation, agricultural industrialization, rural infrastructure construction projects, and policy-oriented grain storage. The Company is also involved in commercial activities, including the construction and operation of industrial parks, property development, as well as trading. As of 31 December 2023, Finance Bureau of Zoucheng City was the ultimate controller of the Company, holding 100% of the Company’s shares.

Rating Rationale

Credit Strengths

Sole SOE focusing on agricultural development in Zoucheng City. SDZC is one of the key SOEs in Zoucheng City and focuses on agricultural development in Zoucheng City. The Company has a clear functional positioning in public-oriented business, especially in the agricultural sector. As the sole state-owned enterprise to focus on local agricultural development, the Company plays an essential role in the construction and operation of the Zoucheng Provincial Agricultural High-tech Industrial Development Zone, fostering the agriculture transformation and upgrading as well as the revitalization of rural economic development in Zoucheng City.

Good track record of receiving government support. As an important entity in agricultural development in Zoucheng City, SDZC has a good track record in receiving government support in terms of capital injections, equity and asset transfers, financial subsidies as well as government special bond support. In order to integrate local resources, the local government transferred the recycled wastes with a book value of RMB5.9 billion to SDZC in 2023 and appointed SDZC as the sole SOE in Zoucheng City to conduct the sales of recycled wastes business. Given the Company's important role in the agricultural development of Zoucheng City, we believe that the local government will continue to provide ongoing support to the Company over the next 12 to 18 months.

Credit Challenges

Increasing exposure to commercial activities with relatively large investment needs. In addition to public activities, SDZC is also engaged in commercial activities such as the construction and operation of industrial parks, property development, as well as trading. While commercial activities generate supplemental income, they may pose higher business and financial risks than public businesses. Due to the expansion of self-operated construction projects, we believe that SDZC's exposure to commercial activities would increase and the Company would have relatively large investment needs in the future.

Fast debt growth with relatively large short-term debt burden. Driven by continuous financing and investment for construction projects, SDZC's total debt level has been growing over the past three years. In addition, the Company has a certain short-term repayment pressure given its relatively high short-term debt burden. Considering the future capital expenditure needs for construction projects, we expect the Company's total debt level would continue to rise over the next 12-18 months. Besides, SDZC's asset liquidity is relatively weak.

Fair access to funding with high reliance on urban commercial banks. SDZC had a high reliance on bank loans for its capital expenditure. Bank loans accounted for around 70% of the total debt. However, majority of bank loans are provided by urban commercial banks in Shandong Province, implying relatively high concentration on urban commercial banks and relatively limited funding channels. The Company also actively strengthens cooperation with policy banks, large state-owned commercial banks and national joint-stock commercial banks to improve its financing channels. In addition, the Company's exposure to non-standard product financing was moderate, accounting for around 10% of its total debt.

Rating Outlook

The stable outlook on SDZC's rating reflects our expectation that Zoucheng City Government's capacity to provide support will be stable, and the Company's characteristics such as its important role in agricultural development of Zoucheng City will remain unchanged over the next 12 to 18 months.

What could upgrade the rating?

The rating could be upgraded if (1) Zoucheng City Government's capacity 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 improved debt management or diversifying the financing channels.

What could downgrade the rating?

The rating could be downgraded if (1) Zoucheng City Government's capacity to provide support weakens; or (2) the Company's characteristics change in a way that weakens the local government's willingness to provide support, such as reduced strategic significance or increased exposure to commercial activities.

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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