

Credit Opinion

30 August 2023

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

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Guangdong Shunde Holding Group Co., Ltd.

Surveillance credit rating report

CCXAP affirms Guangdong Shunde Holding Group Co., Ltd.'s A_g- long-term credit rating, with stable outlook.

Summary

The A_g- long-term credit rating of Guangdong Shunde Holding Group Co., Ltd. ("Shunde Holding" or the "Company") reflects Shunde District Government's (1) very 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 Shunde District Government's capacity to provide support reflects its vital role in Foshan City and Guangdong Province, with strong economic conditions, good fiscal metrics and debt profile.

The rating also reflects the local government's very high willingness to provide support, which is based on the Company's (1) important role in local infrastructure construction and utility services; (2) good track record of receiving government payments; and (3) good access to funding.

However, the Company's rating is constrained by its (1) large exposure to commercial activities with high capital pressure, especially in its property leasing and property development businesses; (2) increasing debt leverage; and (3) medium exposure to contingent liabilities risk.

The stable outlook on Shunde Holding's rating reflects our expectation that the local government's capacity to provide support will remain stable, and the Company will continue to play an important role in local infrastructure construction and public utility services.

Rating Drivers

- Important role in local infrastructure construction and utility services
- Large exposure to commercial activities with high capital pressure
- Good track record of receiving government payments
- Increasing debt leverage
- Good access to funding
- Medium exposure to contingent liabilities risk

Rating Sensitivities

What could upgrade the rating?

The rating could be upgraded if (1) Shunde District's economic prospects and fiscal performance improve and its ability to support the Company increases; and (2) the Company's characteristics change in a way that strengthens the local government's willingness to provide support, such as material reduction of the exposure to risky commercial activities or external guarantee.

What could downgrade the rating?

The rating could be downgraded if (1) Shunde District's economic prospects and fiscal performance deteriorate, reducing its capacity to support the Company; 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, weakened funding ability, or decreased government payments.

Key Indicators

| | 2020FY | 2021FY | 2022FY | 2023Q1 |
|------------------------------|--------|--------|--------|--------|
| Total Asset (RMB billion) | 23.9 | 27.8 | 37.9 | 41.9 |
| Total Equity (RMB billion) | 12.1 | 13.8 | 14.4 | 14.5 |
| Total Revenue (RMB billion) | 2.0 | 2.1 | 2.6 | 0.6 |
| Total Debt/Total Capital (%) | 25.0 | 25.9 | 47.2 | 53.6 |

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

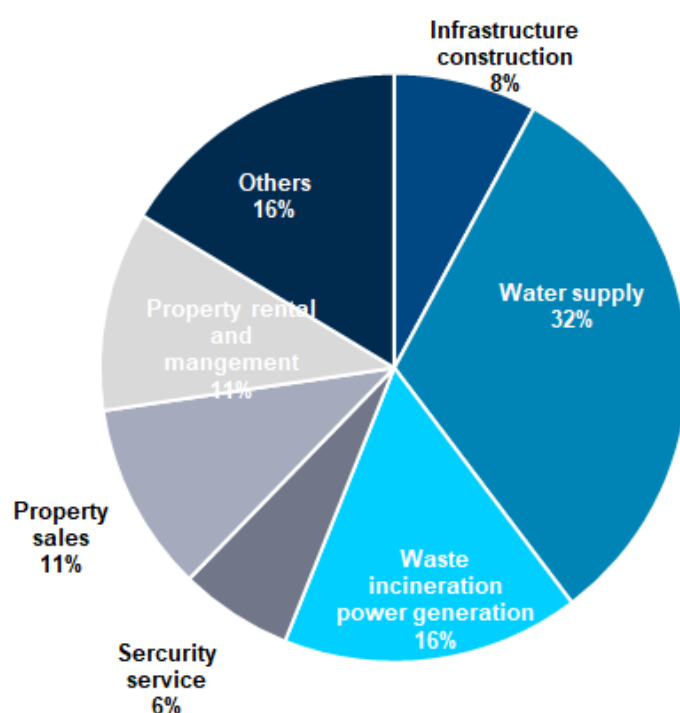
Source: CCXAP research

Corporate Profile

Founded in 2010, Shunde Holding is a local infrastructure investment and financing company ("LIIFC") with the largest total assets in Shunde District. Shunde Holding is responsible for major public infrastructure and welfare projects in the district, including the provision of public utility services such as water supply and waste-to-energy, pipeline network construction, and infrastructure construction such as roads and bridges, and undertaking local environmental protection projects. It also has commercial operations, including property development and operations, equity investments, and security services. As of 31 March 2023, the Company was 90.41% owned by the State-owned Assets Supervision and Administration Commission of Shunde District ("Shunde SASAC") and 9.59% owned by the Guangdong Provincial Department of Finance.

Exhibit 1. Shareholding and organization chart as of 31 March 2023

Source: Company information, CCXAP research

Exhibit 2. Revenue structure in 2022

Source: Company information, CCXAP research

Rating Considerations**Government's Capacity to Provide Support**

We believe Shunde District government has very strong capacity to provide support given its sound economic fundamentals and fiscal strength.

Guangdong Province plays an important role in China's economy, ranking first all year round. It also has good debt management and transparency than most of the other provinces and announced no implicit local government debts in 2022. Foshan City is located in the central part of Guangdong Province and plays a vital role in the economic development of the Guangdong-Hong Kong-Macao Greater Bay Area. Foshan City is dominated by manufacturing, including advantageous industries and emerging industries. In 2022, Foshan City's total Gross Regional Product ("GRP") increased by 2.1% year-over-year ("YoY") to RMB1,269.8 billion,

ranking 3rd in terms of GRP among prefecture-level cities in Guangdong Province. Affected by the tax-refund policy, Foshan City's general budgetary revenue slightly declined from RMB80.7 billion in 2021 to RMB79.7 billion in 2022. Foshan City's tax revenue accounted for 56.3% of general budgetary revenue, while the budgetary self-sufficient ratio rose from 75.4% in 2021 to 78.0% in 2022. Foshan City's government debt increased from RMB185.7 billion in 2021 to RMB227.8 billion in 2022, accounting for 17.9% of its GRP.

Exhibit 3. Key Economic and Fiscal Indicators of Foshan City

| | 2020FY | 2021FY | 2022FY |
|---|---------|---------|---------|
| GRP (RMB billion) | 1,081.6 | 1,215.7 | 1,269.8 |
| GRP Growth (%) | 1.6 | 8.3 | 2.1 |
| General Budgetary Revenue (RMB billion) | 75.4 | 80.7 | 79.7 |
| General Budgetary Expenditure (RMB billion) | 100.3 | 104.0 | 102.1 |
| Local Government Debt (RMB billion) | 152.7 | 185.7 | 227.8 |

Source: Statistic Bureau of Foshan City, CCXAP research

Shunde District is located in the southern part of Guangdong Province and is an important economic center of Foshan City. It represented 33% of Foshan's GRP in 2022, ranking first among the five administrative districts of Foshan City. As a large private economic area focusing on manufacturing, Shunde District is one of the largest production bases for air conditioners, refrigerators, water heaters and disinfection cupboards in China, as well as the largest supply base for rice cookers and microwave ovens in the world. Affected by the pandemic and tax-refund, Shunde District Government's general budgetary revenue slightly declined from RMB27.4 billion in 2021 to RMB26.6 billion in 2022. Its fiscal balance ratio decreased from 103.1% to 98.8% over the same period, but maintaining a relatively high level. As of 31 December 2022, Shunde District's outstanding government debt increased to RMB63.1 billion, with government debt/GRP ratio of 15.1%.

Exhibit 4. Key Economic and Fiscal Indicators of Shunde District

| | 2020FY | 2021FY | 2022FY |
|---|--------|--------|--------|
| GRP (RMB billion) | 359.3 | 406.4 | 416.6 |
| GRP Growth (%) | 4.1 | 8.2 | 0.8 |
| General Budgetary Revenue (RMB billion) | 25.5 | 27.4 | 26.6 |
| General Budgetary Expenditure (RMB billion) | 25.9 | 26.6 | 26.9 |
| Local Government Debt (RMB billion) | 46.1 | 53.9 | 63.1 |

Source: Statistic Bureau of Shunde District, CCXAP research

Government's Willingness to Provide Support

Important role in local infrastructure construction and utility services

Shunde Holding is the most important LIIFC in Shunde District, with a clear strategic role in regional development. The Company is mainly responsible for major public infrastructure and welfare projects in Shunde District, including the provision of public utility services such as water supply and waste-to-energy, pipeline network construction, infrastructure construction such as roads and bridges, and maintenance of highways. We believe that the replacement cost for the Company's role is high as these public services are essential for local residents and regional development.

The Company manages engineering projects assigned by the Shunde District Government and receives agent construction fees based on the construction cost of infrastructure projects. As of 31 March 2023, the Company had 3 infrastructure construction projects under construction, with a total estimated investment of RMB2.4 billion

and an uninvested amount of RMB280 million. Given insufficient infrastructure project under construction and lack of project under planning, the business sustainability is subject to uncertainty. In addition, the Company is in charge of the maintenance of major roads and bridges in Shunde District, receiving stable maintenance fees. In 2022, the Company received maintenance fees of RMB82.7 million. As the infrastructure construction costs and maintenance expenses are mainly supported by the government's fiscal funds, the future investment pressure for both businesses is low.

The Company participates in utility services business via its listed subsidiary Guangdong Shunkong Development Co., Ltd. ("Shunkong Development", Stock Code: 3039.SZ). Shunkong Development is the sole water supplier in Shunde District, with nearly full market coverage of the district. It has a long concession for water supply business until 2045, demonstrating strong sustainability. As of 31 March 2023, the Company had 8 water supply plants with a total water supply capacity of 1.6 million cubic meters per day, serving 10 sub-districts in Shunde District. As of 31 March 2023, the Company is constructing the Shunde Youtan Water Plant Phase II Expansion Project, with an estimated total investment of RMB293 million and uninvested amount of RMB252 million.

Shunkong Development's waste-to-energy business involves incineration power generation, waste treatment, and sludge drying in Shunde District. The Company can process 3,000 tons of domestic waste, 400 tons of sludge from domestic sewage treatment plants, and 300 tons of kitchen waste per day. In 2022, the business showed stable growth momentum, with revenue increasing by 2.3% YoY to 429 million.

Large exposure to commercial activities with high capital pressure

Shunde Holding's major commercial activities include property development, property leasing, security service and strategic investments. We estimate the Company's risk exposure to commercial business is high, accounting for more than 30% of total assets as of end-2022. Most of its commercial businesses are funded through external debt issuance, exerting high capital pressure to the Company. Given the large amount of construction projects, we expect the Company's commercial exposure will continue to increase in the future.

As a major urban comprehensive developer in Shunde District, Shunde Holding is engaged in investment, construction, and operation of leasing properties. It also undertakes the operation of policy-driven properties such as bus terminals, public rental housing, and low-rent housing. As of 31 March 2023, the Company had leased out properties with total area of 545.9 thousand square meters, providing stable rental income. However, the property leasing business has exerted high capital pressure to the Company in the future. As of 31 March 2023, it had 11 operating projects under construction or planning, with a total estimated investment of RMB15.0 billion and uninvested amount of RMB13.0 billion.

Shunde Holding is also engaged in property development through self-operated model. As of 31 March 2023, the Company had spent RMB5.0 billion for the acquisition of 5 land parcels, with total future investment of RMB19.1 billion. The Company also participates in property development via joint ventures. As of 31 March 2023, it had mainly invested in 6 joint venture property projects under construction, with shareholding ranging between 20% and 35%. However, although some of the joint venture's partners are state-owned property developers, part of them are privately-owned property developers, such as Country Garden Holdings Company Limited and Midea Real Estate Group Limited, and the joint venture properties are still in the construction period or the initial stage of operation, exerting uncertainties to investment income. Although the slowdown of property market in China may exert certain business risks to the Company, we expect its investment income will gradually increase after projects completion.

In addition, the Company provides security services to government offices, schools, hospitals and private companies within Shunde District. As the only state-owned security company in the district, the Company is highly competitive and has dispatched more than 2,020 security guards as of 31 March 2023. The Company holds strategic investments including Kaiyuan Securities Co., Ltd., Guangdong Shunde Overseas Chinese Town Industrial Development Co., Ltd., and Guangdong Shunde Rural Commercial Bank Co., Ltd., which are considered to be high-quality and are able to provide considerable investment income to Shunde Holding.

Good track record of receiving government payments

Government payments for Shunde Holding's public infrastructure projects are timely and adequate, as most of its projects are fully supported by the district's fiscal budget. This could largely reduce the capital pressure on Shunde Holding. In addition, the Company continued to receive government support from the Shunde District Government, including capital injections, and subsidies. In 2022, Shunde SASAC injected capital of RMB737 million into the Company. The Company also received subsidies and tax refunds of approximately RMB17.1 million from the local government. Given Shunde Holding's important strategic role, we expect the Company will continue to receive support from the Shunde District Government in the future.

Increasing debt leverage

With ongoing financing for its construction projects and land acquisitions, Shunde Holding has demonstrated a fast debt growth and increasing debt leverage since 2022. The Company's total debt increased from RMB4.8 billion at end-2021 to RMB16.7 billion as of 31 March 2023, while its total capitalization ratio increased from 25.9% to 53.6% over the same period. In addition, the Company's short-term debt servicing pressure remains moderate. As of 31 March 2023, the Company's cash to short-term debt ratio was about 0.8x, and short-term debt accounted for 25% of its total debt. We expect that, given its large future capital needs, the Company will maintain a relatively high debt leverage in the next 12 to 18 months.

Good access to funding

Shunde Holding has good access to funding, including bank loans, bond issuance, and nonstandard financing. As of 31 March 2023, bank loans, bond issuance, and nonstandard financing accounted for about 60%, 4%, and 20% of its total debt, respectively. The Company has a sufficient standby liquidity, granted by diversified domestic policy and commercial banks. As of 31 March 2023, it obtained total credit facilities of RMB20.6 billion, with an unutilized amount of RMB10.5 billion. In the first half of 2023, the Company raised RMB1.0 billion via issuance of 2 tranches of MTNs in the onshore bond market. Through holding a listed subsidiary, the Company also has access to equity financing channels. Taking into account the Company's important status as the sole platform to provide utility services in Shunde District, we expect the Company to maintain access to stable funding and retain good refinancing capabilities.

Medium exposure to contingent liabilities risks

Shunde Holding is subject to medium contingent liabilities risks, driven by its large external guarantees with no counter-guarantee measures. As of 31 March 2023, the Company provided guarantees of around RMB6.7 billion to third parties, accounting for 46.5% of its net assets. Among them, private-owned enterprises accounted for 8.1% of the total guarantees, including Foshan Shunde Xunde Real Estate Co., Ltd., Foshan Shunde Lianhao Development Technology Co., Ltd., and Guangdong Jilong Industrial Park Co., Ltd, the current operating performance of which is stable.

ESG Considerations

Shunde Holding faces environmental risks because it has undertaken infrastructure construction projects and public services. 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.

Shunde Holding bears social risks as it plays a crucial role in the social welfare of the residents in Shunde District by providing public services such as water supply, waste treatment, and leasing of public buildings. As the largest state-owned entity in Shunde District, the Company has also taken several measures to ensure the uninterrupted supply of utility and daily needs of residents during the pandemic control period. For example, due to the impact of the pandemic in 2020, the Company responded to local government policy to provide rent relief for some properties.

In terms of corporate governance, Shunde Holding has established a sound and effective internal control framework and a corporate governance structure in which shareholders, directors, supervisors, senior management team, and internal departments collectively and efficiently perform their duties. The Company is subject to supervision and reporting requirements of the Shunde District Government, which has full control and supervision of the Company's operations.

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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