

## Credit Opinion

8 March 2024

### Ratings

Senior Unsecured Debt Rating	BBB <sub>g</sub> -
Long-Term Credit Rating	BBB <sub>g</sub> -
Outlook	Stable
Category	Corporate
Domicile	China
Rating Type	Solicited Rating

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## Huaiyuan County New Urbanization Construction Co., Ltd

### Initial credit rating report

**CCXAP assigns first-time long-term credit rating of BBB<sub>g</sub>- to Huaiyuan County New Urbanization Construction Co., Ltd, with stable outlook.**

### Summary

The BBB<sub>g</sub>- long-term credit rating of Huaiyuan County New Urbanization Construction Co., Ltd (“HYNC” or the “Company”) reflects the Huaiyuan County Government’s (1) relatively strong capacity to provide support; and (2) extremely high willingness to provide support, based on our assessment of the Company’s characteristics.

Our assessment of the Huaiyuan County Government’s capacity to provide support reflects Huaiyuan County’s gross regional production (“GRP”) ranking first among counties or districts in Bengbu City, but constrained by its relatively weak fiscal metrics.

The rating also reflects the local government’s willingness to provide support, which is based on the Company’s (1) important position as the main infrastructure construction platform in Huaiyuan County; (2) good sustainability of public policy businesses; and (3) solid track record of receiving support from the local government and its parent company.

However, the rating is constrained by the Company’s (1) medium exposure to commercial activities; (2) rapid debt growth driven by large capital expenditure needs; and (3) medium exposure to contingent liability risk.

The stable outlook on HYNC’s rating reflects our expectation that the local government’s capacity to support the Company will remain stable, and the Company will maintain its important position of urban infrastructure development platform of Huaiyuan County.

## Rating Drivers

- Important position as the main infrastructure construction platform in Huaiyuan County
- Good sustainability of public policy businesses
- Medium exposure to commercial activities
- Solid track record of receiving support from the local government and its parent company
- Rapid debt growth driven by large capital expenditure needs
- Diversified funding channels with low exposure to non-standard financing
- Medium exposure to contingent liability risk

## Rating Sensitivities

### What could upgrade the rating?

The rating could be upgraded if (1) the local government's capacity to provide support strengthens; and (2) changes in Company's characteristics enhance local government's willingness to provide support, such as decreased exposure to contingent liability risk and improved debt management.

### What could downgrade the rating?

The rating could be downgraded if (1) the local government's capacity to provide support weakens; or (2) changes in Company characteristics decrease the local government's willingness to provide support, such as reduced regional significance or increase in exposure to commercial activities.

## Key Indicators

	2020FY	2021FY	2022FY	2023Q3
Total Asset (RMB billion)	19.0	28.7	34.9	37.3
Total Equity (RMB billion)	9.3	15.2	15.9	16.1
Total Revenue (RMB billion)	0.9	1.0	1.5	1.1
Total Debt/Total Capital (%)	48.9	44.6	48.9	48.7

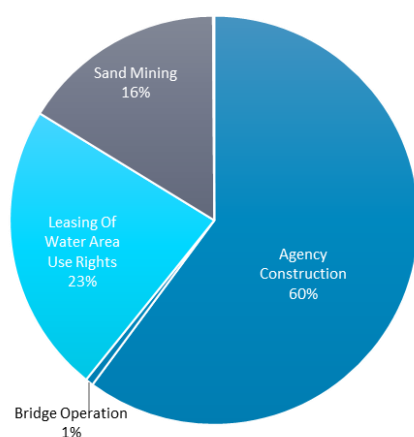
All ratios and figures are calculated using CCXAP's adjustments.

Source: Company data, CCXAP research

## Corporate Profile

HYNC, founded in 2015, is one of the major local infrastructure investment and financing companies ("LIIFCs") in Huaiyuan County. HYNC functions as the core urban infrastructure development platform in Huaiyuan County, mainly engaging in infrastructure construction, bridge operation, as well as affordable housing construction and urban renewal projects. In addition, it also engages in more commercially driven activities, including leasing of water area use rights, sand mining and self-operated project construction. As of 30 September 2023, the State-owned Assets Supervision and Administration Commission of Huaiyuan County People's Government ("Huaiyuan SASAC") was the ultimate controller of the Company, indirectly holding 100% stakes of the Company through Huaiyuan Investment Group Co., Ltd ("HYIG").

## Exhibit 1. Revenue Structure in 2022



Source: Company information, CCXAP research

## Exhibit 2. Shareholding Structure as of 30 September 2023



Source: Company information, CCXAP research

## Rating Considerations

### Government's Capacity to Provide Support

We believe the Huaiyuan County Government has a relatively strong capacity to provide support to the Company, given its GRP ranking first among districts in Bengbu City, but is constrained by its relatively weak fiscal metrics.

Located in the northern part of Anhui Province, Bengbu City is an important comprehensive transport hub in East China. Bengbu City has a good industrial base and has actively developed emerging industries in recent years including silicon-based new materials and new generation technology. Bengbu City has a relatively good economic strength but a moderate financial situation. In 2023, Bengbu City's GRP increased 5.6% year-on-year ("YoY") to RMB211.6 billion. From 2020 to 2022, its GRP decreased slightly from RMB208.2 billion to RMB202.1 billion influenced by external factors and the plan to move manufacturing enterprises into industrial parks. At the same time, the general budgetary revenue of Bengbu Municipal Government increased from RMB15.8 billion to RMB17.4 billion. The fiscal balance ratio of the Bengbu Municipal Government remains moderate. In 2022, the fiscal balance ratio (calculated by general budgetary revenue/general budgetary expenditure) was 48.4%. The debt profile of the Bengbu Municipal Government is relatively weak. At the end of 2022, the

government debt balance increased to RMB62.2 billion, accounting for around 30.9% of GRP and around 147.7% of its total fiscal revenue.

### Exhibit 3. Key Economic and Fiscal Indicators of Bengbu City

	2020FY	2021FY	2022FY
GRP (RMB billion)	208.2	198.9	201.2
GRP Growth (%)	3.0	-2.1	2.0
General Budgetary Revenue (RMB billion)	15.8	16.7	17.4
General Budgetary Expenditure (RMB billion)	39.1	32.9	36.0
Local Government Debt (RMB billion)	45.5	55.6	62.2

Source: Statistic Bureau of Bengbu City, CCXAP research

Huaiyuan County is located in the northern part of Anhui Province and the middle reaches of the Huai River. It is the most populous county among the districts and counties in Bengbu City. The leading industries in Huaiyuan County include machinery and auto parts manufacturing, electronic products, deep processing of agricultural and sideline products, and resource regeneration and comprehensive utilization of straw. Huaiyuan County's GRP ranked the top among all districts/counties in Bengbu City in recent years. In 2022, Huaiyuan County's GRP amounted to RMB35.7 billion, with YoY growth rate of 1.7%. In 2023, Huaiyuan County's GRP further increased by 7.8% YoY to RMB37.9 billion, as a result of a significantly rebound in the local industrial economy after pandemic. Huaiyuan County Government's general budgetary revenue kept increasing over the past three past years, which increased to RMB2.8 billion in 2023 from RMB2.3 billion in 2020. However, Huaiyuan County has a relatively weak fiscal profile. In 2022, its fiscal balance ratio was 33.7% and stability ratio was around 50.4%, reflecting a high reliance on fiscal support from higher-tier governments. As of 31 December 2022, the outstanding debt of Huaiyuan County Government was RMB8.9 billion, accounting for 24.9% of its GRP.

### Exhibit 4. Key Economic and Fiscal Indicators of Huaiyuan County

	2020FY	2021FY	2022FY
GRP (RMB billion)	42.5	35.6	35.7
GRP Growth (%)	-1.1	-12.0	1.7
General Budgetary Revenue (RMB billion)	2.3	2.5	2.6
General Budgetary Expenditure (RMB billion)	7.6	7.0	7.8
Local Government Debt (RMB billion)	4.8	7.9	8.9

Source: Statistic Bureau of Huaiyuan County, CCXAP research

## Government's Willingness to Provide Support

### Important position as the main infrastructure construction platform in Huaiyuan County

HYIG, the Company's parent company, is the largest LIIFC in Huaiyuan County in terms of total assets and the most important infrastructure construction and state-owned assets operation entity in the Huaiyuan County. In addition, HYIG has the largest business scope and strongest comprehensive strength in Huaiyuan County as most of the major LIIFCs in the region are its subsidiaries. As one of the core subsidiaries of HYIG, HYNC plays a vital role in the infrastructure construction of Huaiyuan County. HYNC conducts many public-policy activities for the local government, including urban infrastructure construction, affordable housing construction and shanty town renovation, which carry significant strategic importance for the government and benefit the local social and economic development. Considering its strategic importance in undertaking public-policy projects in Huaiyuan

County, we believe the Company will not be easily replaced by other local state-owned enterprises in the foreseeable future.

### **Good sustainability of public policy businesses**

As the core operating entity in Huaiyuan County, HYNC is responsible for the provision of public services and implementation of urban development activities in the region, such as agent construction and bridge operation. The Company has sufficient construction projects in the pipelines, ensuring its sustainability of public policy businesses but exerting certain capital expenditure pressure.

The Company conducts infrastructure construction business mainly through an agency construction model. Under the agent construction model, HYNC enters into an agency construction agreement with the related departments of the Huaiyuan County Government and the related departments will pay the total cost plus a few percentage markups after examining the projects. As of 30 June 2023, the Company had invested a total of RMB6.2 billion into 6 infrastructure construction projects under construction, including the construction of roads, rural renovation projects, and urban renewal projects. Meanwhile, the Company had 3 proposed projects with a total planned investment of RMB2.1 billion including shantytown construction projects and urban renewal projects. The Company has sufficient project reserves that support good stability and sustainability of the infrastructure construction business. Besides, some of the Company's infrastructure projects can be supported by government special bonds, which can further alleviate its debt burden.

HYNC is also responsible for bridge operation business. The income from this business is mainly generated from the operation charging rights of Jingxu Huaihe River Bridge in Huaiyuan County. The operation period is as long as 26 years, starting from 1 January 2005 to 31 December 2030. As the Company does not charge the local vehicles, the revenue of bridge operation business is still small and under deficit. In light of its public welfare nature and the importance to local social and economic development, the bridge operation business receives operating subsidies from the local government every year.

### **Medium exposure to commercial activities**

We consider HYNC to have medium exposure to commercial activities, such as leasing of water area use rights, sand mining and self-operated project construction, as its market-driven businesses accounted for around 20% to 25% of its total assets. These activities have been a good supplement to the Company's revenue but could exert certain funding and business risks. We expect the Company's exposure to commercial activities will continue to rise following its increasing investment in self-operated projects in the future.

The leasing of water area use rights business is one of the Company's major sources of income, which accounted for 23.0% of the total revenue in 2023Q3 with strong profitability. In 2019, the local government transferred water area use rights of Sifang Lake, Qianhe Lake and Manli Lake, totaling 143,955 mu, to the Company without compensation, with book value of RMB2.8 billion at end-2023Q3. The Company signed a water area lease contract with a government related department and the lease term is 10 years, from 1 January 2020 to 31 December 2029. The Company received annual leasing fee of RMB350.0 million in the first five year, and the leasing fee increases by 0.5% annually from the sixth year, contributing stable revenue for the Company in the future.

The Company broadened its business scope to sand mining business in 2022. In 2021, the local government transferred sand mining rights of the river segment between Zhanglou Village and Zhouwang Village to the Company without compensation, with book value of RMB2.9 billion at end-2023Q3. The sand mining business

generated stable income, which amounted to RMB234.3 million in 2022 and RMB175.7 million in 2023Q3. However, the gross profit margin of the business was as low as 6.9% both in 2022 and 2023Q3.

Meanwhile, the Company also engaged in the construction and operation of self-operated projects, mainly industrial parks projects which aims to support local industries and supplement its income. As of 30 June 2023, the Company had 2 industrial parks construction projects under construction with a total planned investment of RMB3.2 billion and an uninvested amount of RMB1.1 billion and 2 industrial parks construction projects under planning with a total planned investment of RMB1.0 billion. The Company is expected to achieve fund balancing through factory sales and rentals after project completion. However, the relatively large scale of investment needs may bring more pressure on the capital expenditure of the Company. In addition, there is uncertainty about the realization of future returns and its investment return period is usually long.

### **Solid track record of receiving support from the local government and its parent company**

As an important infrastructure construction platform in Huaiyuan County, HYNC has received recurring support from the local government and HYIG, including financial subsidies, asset injections and capital injections. From the perspective of asset injections, the Company received the operation charging rights of Jingxu Huaihe River Bridge in Huaiyuan Count from the Huaiyuan County Government with an operation period of 26 years, starting from 1 January 2005 to 31 December 2030. In 2019, the Huaiyuan County Government transferred water area use rights of Sifang Lake, Qianhe Lake and Manli Lake, totaling 143,955 mu, to the Company without compensation. In 2021, the Huaiyuan County Government transferred RMB3.3 billion of sand mining rights and RMB2.1 billion of forest rights without compensation to the Company to enhance its capital strength and business scope. In 2022, the Company has received capital injections of RMB300 million from HYIG, allowing the Company to be engaged in capital-intensive and large-scale projects. HYNC also has a good track record of receiving government payments. From 2020 to 2022, the Company continuously received government subsidies with a total amount of around RMB1.0 billion. In light of HYNC's important strategic role in the region, we expect the Company will receive ongoing support from the government and its parent in the future.

### **Exhibit 5. Government Support from 2020 to 2022**

<b>(RMB million)</b>	<b>2020FY</b>	<b>2021FY</b>	<b>2022FY</b>
Government Subsidies	303	310	390
Asset Injections	116	5,404	-
Capital Injections	-	-	300
<b>Total</b>	<b>419</b>	<b>5,714</b>	<b>690</b>

Source: Company information, CCXAP research

### **Rapid debt growth driven by large capital expenditure needs**

Due to the continuous investment in infrastructure construction projects and commercial activities, HYNC's total debt has been growing over the past three years. As of 30 September 2023, the Company's total debt increased from RMB8.9 billion at end-2020 to RMB15.3 billion, with the total capitalization ratio of 48.7%. In addition, the Company's debt maturing structure is reasonable. As of 30 September 2023, its short-term debt accounted for about 13.1% of its total debt, and cash to short-term debt ratio was 0.4x, indicating certain short-term debt servicing pressure. Considering the Company's ongoing investment needs for self-operated infrastructure construction projects in the future, we expect that the Company may rely on external financing to meet its capital expenditures and the Company's debt leverage will remain at a relatively high level in the next 12 to 18 months.

### **Weak asset liquidity**



In addition, HYNC has weak asset liquidity. As of 30 September 2023, the Company's inventories, total receivables, and intangible assets accounted for 89.3% of its total assets. The inventories are mainly investment costs for infrastructure construction projects, forest rights assets, and land use rights, while the total receivables are mainly unreceived payments from the local government and other local state-owned enterprises, which are considered low liquidity. The intangible assets mainly consist of operation charging rights, sand mining rights and leasing of water area rights, which could generate certain amount of supplemental revenue.

### **Diversified funding channels with low exposure to non-standard financing**

The Company had access to various sources of funding, including bank loans, onshore and offshore bond financing and non-standard financing. As of 30 September 2023, around 65.8% of the Company's debt financing was provided by domestic banks, with total credit facilities of RMB13.6 billion and available credit facilities of RMB1.9 billion, indicating a moderate liquidity buffer. Meanwhile, HYIG, the Company's parent company, has total credit facilities of RMB60.6 billion with an unutilized amount of RMB6.1 billion, providing the Company certain backup liquidity support. The Company also has a good track record for fund-raising activities in debt capital markets. From 2020 to 2023, the Company raised RMB3.7 billion in total through issuance of 6 onshore bonds, including special bonds and private corporate bonds, with average coupon rate of about 6.4%. It also has an access to offshore bond market. In March 2022, HYNC issued one tranche of three-year offshore bond raising USD100 million. In addition, the Company's exposure to non-standard financing is low, accounting for around 4.9% of total debt financing as of 30 September 2023. Considering relatively large capital expenditure of its infrastructure construction projects, we expect the Company will continue to rely on external financing.

### **Medium exposure to contingent liability risk**

The Company bears certain contingent risk resulting from relatively large external guarantees, which could potentially increase its repayment obligations. As of 30 September 2023, the Company's external guarantees amounted to RMB7.4 billion, accounting for 46.0% of its net assets. 97.8% of the external guarantees were provided to local state-owned enterprises ("SOEs") in Huaiyuan County and the remaining external guarantees were provided to local private-owned enterprises. Given the relatively large amount of external guarantees with no counter-guarantee measures, the Company is subject to certain contingent liability risk. Nevertheless, we estimate most of these local SOEs are likely to be supported by the local government when necessary, so that contingent risk would be controllable.

## **ESG Considerations**

The Company is subject to environmental laws and regulations governing air pollution, noise emissions, hazardous substances, water and waste discharge and other environmental matters issued by the national governmental authorities. HYNC assumes environmental risks for its infrastructure projects. Such risks could be mitigated by conducting environmental studies and detailed planning prior to the commencement of projects and close supervision during construction.

HYNC is also exposed to social risks as it implements public-policy initiatives by building public infrastructure in Huaiyuan County. Demographic changes, public awareness and social priorities shape government's development strategy, and it will affect the government's propensity to support the Company.

The Company's governance considerations are also material as it is subject to oversight and reporting requirements to the local government, reflecting its public-policy role and status as a government-owned entity. HYNC believes that it is in compliance in all material respects with the applicable governmental regulations,

rules and executive orders in each jurisdiction in which it operates. The Company maintains regular communication with local governments and regulatory authorities through its management team or representatives, ensuring compliance with the requirements and conditions for obtaining and maintaining the licenses, concessions, permits, or certificates.

### **Structural considerations**

HYNC's senior unsecured debt rating is equivalent to its long-term credit rating. We believe that government support will flow through the Company given its key roles in the development of Huaiyuan County, thereby mitigating any differences in an expected loss that could result from structural subordination.

### **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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