

Credit Opinion

29 May 2024

Ratings

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

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Changxing Urban Construction Investment Group Co., Ltd.

Surveillance credit rating report

CCXAP upgrades Changxing Urban Construction Investment Group Co., Ltd.'s long-term credit rating to BBB_g+, with stable outlook.

Summary

CCXAP has upgraded the long-term credit rating of Changxing Urban Construction Investment Group Co., Ltd. ("CUCI" or the "Company") to BBB_g+

from BBB_g, with stable outlook. The rating upgrade is based on the improving regional strength of Changxing County, which strengthens the local government's capacity to support the Company. It also reflects the Company's strong position in undertaking infrastructure construction and public services in Changxing County.

The long-term credit rating of CUCI reflects (1) Changxing County Government's strong capacity to support, and (2) the local government's extremely high willingness to support, based on our assessment of the Company's characteristics. Our assessment of Changxing County Government's capacity to support reflects its ranking of 55th among the Top 100 Counties in China in 2023, with good economic strength and moderate fiscal metrics.

The rating also reflects the local government's willingness to support, which is based on the Company's (1) strong position in undertaking infrastructure construction and public services in Changxing County; (2) access to diversified funding channels; and (3) good track record of receiving government payments.

However, the rating is constrained by the Company's (1) increasing operating risks arising from diversified business segments; (2) medium contingent liability risk from external guarantees provided to other local SOEs; and (3) relatively high debt leverage and moderate asset liquidity.

The stable outlook on CUCI's rating reflects our expectation that the local government's capacity to support will remain stable, and the Company will maintain its important role in the public welfare functions in Changxing County.

Rating Drivers

- Strong position in undertaking infrastructure construction and public services in Changxing County
- Good track record of receiving ongoing government payments
- Increasing operating risks arising from diversified business segments
- Relatively high debt leverage and moderate asset liquidity Large
- Access to diversified funding channels
- Medium contingent liability risk from external guarantees provided to other local SOEs

Rating Sensitivities

What could upgrade the rating?

The rating could be upgraded if (1) the local government's capacity to support strengthens; or (2) the Company's characteristics change in a way that strengthens the local government's willingness to support, such as improvement in debt management or assets quality.

What could downgrade the rating?

The rating could be downgraded if (1) the local 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 decrease in its strategic significance; decrease in government payments; or increase in exposure to commercial activities.

Key Indicators

	2021FY	2022FY	2023FY
Total Asset (RMB billion)	70.6	76.5	80.3
Total Equity (RMB billion)	32.7	32.9	32.6
Total Revenue (RMB billion)	3.2	3.3	3.4
Total Debt/Total Capital (%)	49.9	52.7	55.6

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

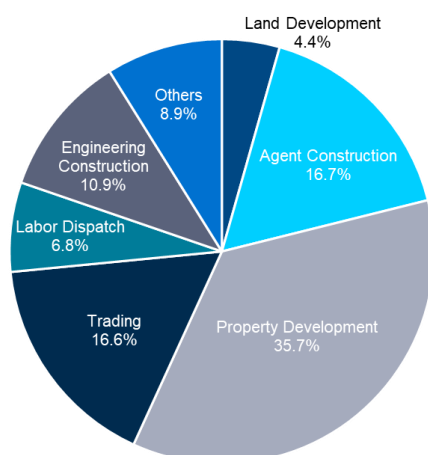
Source: Company data, CCXAP research

Corporate Profile

CUCI, formerly known as Changxing Urban Construction Co., Ltd., was established on 21 December 2007, CUCI is one of the key local infrastructure investment and financing companies ("LIIFCs") in Changxing County, Huzhou City. The Company mainly engages in trading, infrastructure construction, property development, primary land consolidation and city operations, including water supply, assets leasing and car park operation in Changxing County.

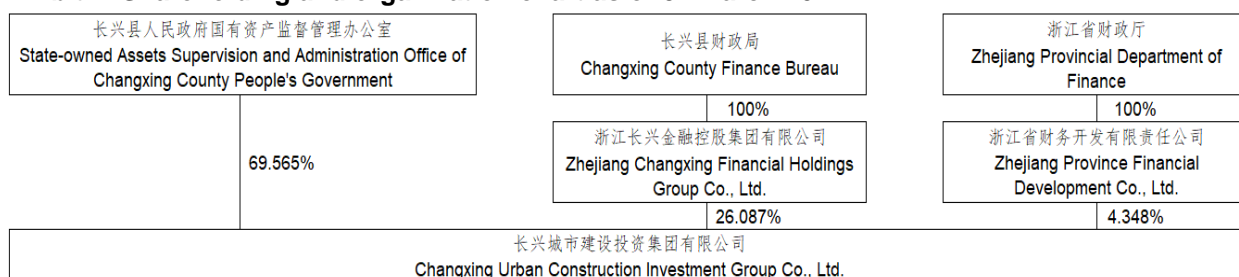
As of 31 March 2024, the State-owned Assets Supervision and Administration Office of Changxing County People's Government ("Changxing SASAO") and Zhejiang Changxing Financial Holdings Group Co., Ltd. held 69.6% and 26.1% of the Company's shares, respectively, while Zhejiang Province Financial Development Co., Ltd. held the remaining 4.3%. Changxing SASAO is the ultimate controller of the Company.

Exhibit 1. Revenue structure in 2023



Source: Company information, CCXAP research

Exhibit 2. Shareholding and organization chart as of 31 March 2024



Source: Company information, CCXAP research

Rating Considerations

Government Capacity to Support

We believe that Changxing County Government has a strong capacity to provide support given its status as the 55th Top 100 Economic Counties in China in 2023, with good economic strength and moderate fiscal metrics.

Located in the northern part of Zhejiang Province, Huzhou City is the node city connecting the north and south areas of the Yangtze River Delta region. Huzhou City has four leading industries including information technology, high-end equipment, health and tourism. It has achieved a significant increase in gross regional product (“GRP”) over the past three years. In 2023, Huzhou City recorded a GRP of RMB401.5 billion, increasing by 5.8% year-over-year (“YoY”). Due to the economic recovery and industry growth, Huzhou Municipal Government’s general budgetary revenue increased from RMB38.7 billion in 2022 to RMB41.1 billion in 2023. It also has good fiscal stability, with tax income accounting for around 90% of general budgetary revenue for the past three years. Its fiscal balance remained at a moderate level, with general budgetary revenue to general budgetary expenditure ratio of 67.6% in 2023. However, Huzhou Municipal Government’s debt burden was large with an outstanding direct government debt of RMB136.4 billion at end-2023, accounting for 34.0% of its GRP and 98.6% of its total fiscal revenue.

Exhibit 3. Key Economic and Fiscal Indicators of Huzhou City

	2021FY	2022FY	2023FY
GRP (RMB billion)	364.5	385.0	401.5
GRP Growth (%)	9.5	3.3	5.8
General Budgetary Revenue (RMB billion)	41.4	38.7	41.1
General Budgetary Expenditure (RMB billion)	52.4	60.2	60.7
Local Government Debt (RMB billion)	102.3	118.9	136.4

Source: Statistics Bureau of Huzhou City, CCXAP research

Changxing County is the second largest county, in terms of GRP, in Huzhou City. According to CCID Consulting, Changxing County ranked 55th among the Top 100 Economic Counties in China in 2023. It also ranked third among the top 100 tourism comprehensive strength counties for five consecutive years. The pillar industries of Changxing County are textile, cement and battery manufacturing industries. In addition, Changxing County has improved its industrial structure by strategically promoting emerging industries, such as new type battery and new energy vehicle, and has developed a sizeable leisure facility, namely Longmont, with a total investment of around RMB25 billion. Changxing County has a developed private economy, at the end of 2023, there were 901 private-owned enterprises, accounting for 90.7 % of industrial enterprises above designated size; and there was a total of 11 listed companies in Changxing County, with a total IPO financing of RMB2.3 billion. In 2023, Changxing County recorded a GRP of RMB89.4 billion, increasing by 6.5% YoY, representing around 22.3% of Huzhou City's GRP. We believe that the sustainable economic development of Changxing County provides a sound external environment for the Company's business development. Its general budgetary revenue also increased from RMB8.2 billion in 2022 to RMB8.7 billion in 2023. It also has good fiscal quality, with tax income accounting for around 86.2% of general budgetary revenue. However, Changxing County had an increasing debt burden, as of end-2023, Changxing County Government's outstanding direct debt amounted to RMB20.2 billion, about 22.6% of its GRP and 112.1% of its total fiscal revenue.

Exhibit 4. Key Economic and Fiscal Indicators of Changxing County

	2021FY	2022FY	2023FY
GRP (RMB billion)	80.1	85.3	89.4
GRP Growth (%)	9.5	4.2	6.5
General Budgetary Revenue (RMB billion)	8.3	8.2	8.7
General Budgetary Expenditure (RMB billion)	10.2	10.5	12.0
Local Government Debt (RMB billion)	17.7	19.1	20.2

Source: Statistics Bureau of Changxing County, CCXAP research

Government Willingness to Support**Strong position in undertaking infrastructure construction and public services in Changxing County**

There are four major LIIFCs to support the development and operation of Changxing County. Each has a clear position under the local government's planning. Among them, CUCI is one of the most important investment and construction entities in Changxing County and has mainly undertaken public activities such as infrastructure construction, primary land consolidation, and water supply. Given the Company's strong position in local development and the high sustainability of its public services, we believe the Company is unlikely to be replaced by other entities in the foreseeable future.

CUCI is one of the key infrastructure constructors with a strong regional position in Changxing County. Currently, the Company is mainly responsible for the infrastructure construction in the Old Town District and Longshan New District under the agent-construction model. As of 31 March 2024, the Company had 10 infrastructure construction projects under construction, with a total estimated investment of RMB762.5 million, and an uninvested amount of RMB417.5 million; it also had 2 infrastructure construction projects under planning, with a total estimated investment of RMB115.0 million. These projects mainly include the construction of schools, hospital, and environment improvement projects. Given the sufficient infrastructure projects in the pipeline and the large infrastructure construction demand in Changxing County, we believe the Company's infrastructure construction business has good sustainability.

CUCI also has a strong regional position in the primary land consolidation of Changxing County. The Company's business scope of primary land consolidation business covers Longshan New District, Huilongshan New District and the Old Town District. As of 31 March 2024, the Company completed the consolidation of 366.5 mu land parcels that have not yet been sold. The Company also has sufficient project reserves for its primary land consolidation. There were five land consolidation projects under development with an area of 11,404 mu and an invested amount of RMB2.5 billion. However, the primary land consolidation business is largely susceptible to market conditions and government policies.

The Company has participated in water supply projects through its subsidiary, such projects include production and construction of water supply and drainage, and installation of water engineering. In 2023, the Company has 2 new water supply plants and currently has 4 water plants in operation. Besides, the Company has 4 water supply stations with a 1,014-kilometer network and a daily water supply capacity of around 85,000 tons/day, serving 70,000 residents. The operating area of its water supply business has also expanded to 450 square kilometres as of 31 March 2024, compared with 358 square kilometres at the end of 2022. With the completion of its developing projects, we expect that the Company's public welfare function will be strengthened, suggesting stronger strategic importance and stronger governmental support.

Good track record of receiving ongoing government payments

The local government provides strong support, in terms of capital injection, assets injection and financial subsidies, to the Company to support its business development and enhance its assets. In 2021, the government injected 35 reservoir sand mining rights into the Company, with an estimated value of RMB2.8 billion. In 2022, the Company has received seedling assets with a value of RMB731.0 million from the local government. In 2023, the local government also injected civil air defense assets of RMB1.6 billion into its subsidiary. From 2021 to 2023, the Company received RMB2.6 billion in government subsidies and a fiscal interest discount of RMB960.0 million to support its operation. The local government also injected sandstone assets operation rights, outdoor advertising spaces franchise rights as well as parking management rights within the main urban area of Changxing County, enriching the Company's business segments. Given CUCI's important role in the development of Changxing County, we expect the local government will continue to provide ongoing support to the Company.

Increasing operating risks arising from diversified business segments

Apart from the primary business segments, CUCI has also diversified into other market-oriented businesses since 2017, such as trading, property development, and sandstone mining. Overall, the proportion of commercial business assets is around 25% of the Company's total assets, indicating that the overall commercial business risk is moderate. We also expect that the diversified business layout can enrich its income source. However,

some of these businesses such as property development are affected by the downturn of China's property market, which may adversely affect the Company's profitability.

CUCI has engaged in property development since December 2017. As of 31 March 2024, the Company held 6 properties with a remaining saleable area of 106.6 thousand sqm, which is sufficient to support the Company's revenue in the short run. In addition, the Company had 3 property projects under construction, with a total planning construction area of 471.8 thousand sqm, and an uninvested amount of RMB1.2 billion. The property sales income is the largest contributor to the Company's revenue. In 2023, the revenue from this business accounted for 35.7% of the total revenue. In addition, except for the Lanyuan project, all of the Company's property projects are in the form of resettlement housing and commercial housing. As of 31 March 2024, the Company's resettlement housing sales rate was in the range of 71% to 90%, ensuring the payment collection for this business. However, the large investment needs will bring certain capital expenditure pressure to the Company, and uncertainty exists in this business as it is highly subject to local government planning and the local real estate market, which may also exert higher volatility during the downturn of China's property market.

CUCI gained a 30-year franchise right for sandstone mining in Changxing County. The Company's sandstone mining covers total sandstone reserves of 146.3 million tons and exploitable amounts of 52.3 million tons. Due to high amortization costs and short operation time, the Company incurred large gross losses from the business, encumbering its overall profitability. CUCI has engaged in car park operations since November 2018. As of 31 March 2024, the Company owned 2,446 on-street parking spaces and 8 parking lots in operation. The Company also has 11 parking lots under development, which are expected to provide 4,316 parking spaces and 500 charging piles to the Company. The Company also earns rental income by leasing self-owned investment properties, including commercial complexes and residential properties. As of 31 March 2024, the Company had 2 self-operated projects under construction, which are expected to be completed in 2024, with a total planned investment amount of RMB2.1 billion and an uninvested amount of around RMB1.6 billion.

For the trading segment, the Company mainly provides building materials and coals to local corporates. The trading business contributed around 16.6% of the Company's revenue in 2023; the gross profit margin of this business has improved, recording 4.4% in 2023, compared with 1.3% in 2022. The Company's trading business showed a relatively high concentration risk as its top 5 suppliers and customers accounted for around 94.5% and 82.2% of its purchasing and sales amount, respectively, increasing uncertainties in this business.

Relatively high debt leverage and moderate asset liquidity

The Company's total debt continued to increase due to ongoing investment needs. From 2022 to 2023, the Company's total debt increased from RMB36.6 billion to RMB40.8 billion, and its total capitalization ratio was at a relatively high level of around 55.6% at the end of 2023. In addition, the Company has a relatively high short-term debt servicing pressure, with a short-term debt to total debt ratio of 28.6% and its cash to short-term debt ratio was 0.6x at end-2023. We expect the Company's debt leverage to remain at a high level in the next 12 to 18 months, given its large capital expenditure needs for its extensive construction projects in the pipeline.

The Company's asset liquidity is moderate as they are mainly inventories with weak liquidity. As of 31 March 2024, the inventories amounted to RMB34.5 billion, accounting for 43.0% of total assets, and mainly consisted of construction costs caused by infrastructure construction projects. The moderate liquidity asset may undermine the Company's financing flexibility, which is credit-negative. Besides, the Company has pledged some assets for loans, accounting for around 7.3% of total assets as of the end of 2023.

Access to diversified funding channels

The Company's large investment needs can be mitigated by its diversified financing channels. The Company has access to various sources of funding, including bank loans, onshore and offshore bond financing and non-standard financing. As of end-2023, the Company had total credit facilities of RMB29.6 billion, of which the unutilized amount was about RMB7.8 billion. The Company also has good access to the debt markets. From 2021 to 2023, the Company and its subsidiaries raised a total of RMB16.5 billion through the onshore debt market; and had raised USD600 million through the offshore debt market. Besides, the Company's exposure to non-standard financing is relatively low, accounting for about 10% of total debt at end-2023.

Medium contingent liability risk from external guarantees provided to other SOEs

The Company is exposed to a medium contingent liabilities risk. At the end of 2023, the Company recorded an external guarantee amount of RMB9.4 billion, accounting for 28.9% of its total equity. Those guaranteed entities are the state-owned enterprises ("SOE") in Changxing County, without counter-guarantee measures. The credit risk of the Company and other local SOEs might be heightened if one guaranteed entity suffers from credit issues.

ESG Considerations

CUCI is exposed to environmental risks because it has undertaken infrastructure construction and utility projects. Such risks could be moderated by conducting environmental studies and planning before the commencement of projects, and close supervision during the construction phase. Since 2021, CUCI issued two green USD bonds and three green corporate bonds on both onshore and offshore markets. The issuance of green bonds by CUCI is an important example of promoting the innovative development of green finance, which can reduce its environmental risks.

In terms of social concerns, CUCI plays a crucial role in the social welfare of the residents in Changxing County by providing utility services, including water supply, sewage treatment, education, and car park operation. As an important state-owned entity in Changxing County, the Company has also launched multiple measures to ensure the provision of utility and daily needs of the residents during the pandemic control period.

In terms of corporate governance, CUCI has established a sound and effective internal control framework, and has also set up a corporate governance structure, with the shareholders, directors, supervisors, senior management team and internal departments performing their duties collectively and efficiently. The Company is subject to oversight and reporting requirements to the Changxing SASAO, which has full control and supervision of the Company's operation.

Structural considerations

The rating of the senior unsecured bonds is equal to CUCI's long-term credit rating. We believe that government support will flow through the Company given its important role in undertaking public services in Changxing 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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