

Credit Opinion

6 September 2024

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

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Taizhou Luqiao State-owned Assets Development Group Co., Ltd.

Surveillance credit rating report

CCXAP affirms Taizhou Luqiao State-owned Assets Development Group Co., Ltd.'s long-term credit rating at BBB_g+, with stable outlook.

Summary

The BBB_g+ long-term credit rating of Taizhou Luqiao State-owned Assets Development Group Co., Ltd. ("LSAD" or the "Company") reflects (1) Luqiao District Government's strong capacity to provide support; and (2) the local government's extremely high willingness to provide support, based on our assessment of the Company's characteristics.

Our assessment of Luqiao District Government's capacity to provide support reflects its relatively good comprehensive strength, ongoing economic growth, and good fiscal profile.

The rating also reflects the local government's willingness to provide support, which is based on the Company's (1) status as the most important infrastructure construction and state-owned assets operation entity in Luqiao District; (2) high sustainability of public policy businesses; and (3) good track record of receiving government support.

However, the Company's rating is constrained by its (1) medium exposure to commercial activities; (2) high debt leverage and weak asset liquidity; and (3) medium exposure to external guarantees, with moderate contingent liability risk.

The stable outlook on LSAD's rating reflects our expectation that the local government's capacity to provide support will remain stable, and the Company will maintain its status as the most important infrastructure construction and state-owned assets operation entity in Luqiao District.

Rating Drivers

- Status as the most important infrastructure construction and state-owned assets operation entity in Luqiao District
- High sustainability of public policy businesses
- Good track record of receiving government support
- Medium exposure to commercial activities
- High debt leverage and weak asset liquidity
- Medium exposure to external guarantees, with moderate contingent liability risk

Rating Sensitivities

What could upgrade the rating?

The rating could be upgraded if (1) local 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 materially decrease in its exposure to commercial activities.

What could downgrade the rating?

The rating could be downgraded if (1) local 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 decrease in its regional importance, materially decrease in government payments, or deteriorated debt management.

Key Indicators

	2021FY	2022FY	2023FY
Total Asset (RMB billion)	71.8	76.7	85.6
Total Equity (RMB billion)	26.1	26.0	26.5
Total Revenue (RMB billion)	1.4	1.5	1.8
Total Debt/Total Capital (%)	58.4	61.8	65.8

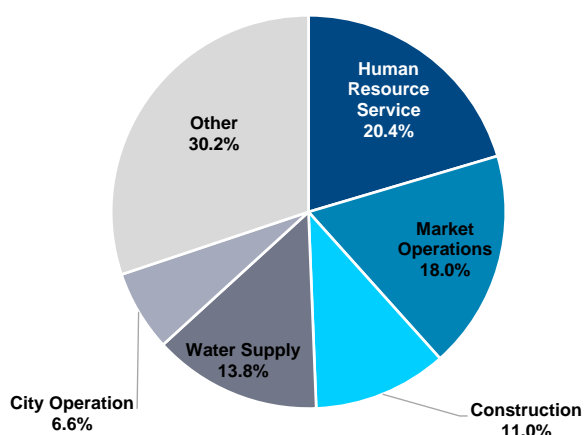
All ratios and figures are calculated using CCXAP's adjustments.

Source: Company data, CCXAP research

Corporate Profile

Founded in 2000, LSAD is the most important local infrastructure investment and financing company ("LIIFC") in Luqiao District, Taizhou City. The Company mainly engages in infrastructure construction, resettlement housing construction, water supply and sewage treatment businesses, as well as commercial businesses such as property development, property leasing, trading, and human resources service in Luqiao District. As of 31 December 2023, the Company is wholly owned and directly controlled by Luqiao District State-owned Assets Working Center.

Exhibit 1. Revenue structure in 2023



Source: Company information, CCXAP research

Rating Considerations

Government's Capacity to Provide Support

We believe Luqiao District Government has a strong capacity to provide support given its relatively good comprehensive strength, ongoing economic growth, and good fiscal profile.

Zhejiang Province is one of the most economically developed provinces in China, and its comprehensive economic strength and private economy leads in China. In 2023, the gross regional product ("GRP") of Zhejiang Province was RMB8.3 trillion, ranking 4th among all provinces in China, with a year-on-year ("YoY") increase of 6.0%. In 2023, its general budgetary revenue reached RMB0.9 trillion, ranking 3rd among all provinces in China.

Taizhou City, as one of the key cities in the Yangtze River Delta Economic Area, enjoys a leading position in terms of economic development among all cities in Zhejiang Province. Taizhou City has outstanding transportation infrastructure, making it an important transportation hub in central Zhejiang Province. Taizhou City has a well-developed manufacturing industry, and has formed six pillar industries, such as automobiles and motorcycle accessories, pharmaceutical chemicals, sewing equipment, marine equipment, household appliances, and plastic molds. Taizhou City has a well-developed private economy. At the end of 2024Q1, there were 73 listed companies in Taizhou City, more than 90% of which were private-owned enterprises, such as Tianshan Aluminum Group Co., Ltd and Shentong Express Co., Ltd., providing a good foundation for its economy and taxation. In 2023, Taizhou City's GRP increased by 4.5% YoY to RMB624.1 billion, ranking 6th among all prefecture-level cities in Zhejiang Province. Benefited from economic recovery and industrial development, the Taizhou Municipal Government's general budgetary revenue increased from RMB44.1 billion in 2022 to RMB49.4 billion in 2023. However, Taizhou City's debt profile is modest and its outstanding governmental debt amounted to RMB182.2 billion at end of 2023, equivalent to 29.2% of its GRP.

Exhibit 2. Key economic and fiscal indicators of Taizhou City

	2021FY	2022FY	2023FY
GRP (RMB billion)	578.6	604.1	624.1
GRP Growth (%)	8.3	2.7	4.5
General Budgetary Revenue (RMB billion)	45.5	44.1	49.4
General Budgetary Expenditure (RMB billion)	73.5	83.5	83.7
Local Government Debt (RMB billion)	139.7	160.6	182.2

Source: Statistics Bureau of Taizhou City, CCXAP research

Luqiao District is one of the three main urban areas of Taizhou City, with relatively good comprehensive strength. In 2023, it ranked 56th by comprehensive strength among top 100 districts in China. With developed private economy and regional characteristics, it has formed 4 pillar industries, including commerce and trade, finance, automobiles, and metal resource recycling. From 2022 to 2023, the GRP of Luqiao District increased from RMB75.7 billion to RMB78.3 billion. With the ongoing economic growth, Luqiao District Government's general budgetary revenue also increased from RMB5.0 billion in 2022 to RMB5.3 billion in 2023. Besides, Luqiao District has good fiscal profile, as reflected by its high fiscal stability and good fiscal self-sufficiency. In 2023, its tax income accounted for 85.2% of general budgetary revenue and its fiscal balance ratio remained high at 94.5%. Luqiao District Government reported outstanding governmental debt of RMB19.4 billion at end-2023, representing 21.6% of GRP.

Exhibit 3. Key economic and fiscal indicators of Luqiao District

	2021FY	2022FY	2023FY
GRP (RMB billion)	71.7	75.7	78.3
GRP Growth (%)	8.3	3.7	6.0
General Budgetary Revenue (RMB billion)	4.3	5.0	5.3
General Budgetary Expenditure (RMB billion)	4.8	5.4	5.6
Local Government Debt (RMB billion)	15.1	16.3	19.4

Source: Statistics Bureau of Luqiao District, CCXAP research

Government's Willingness to Provide Support**Status as the most important infrastructure construction and state-owned assets operation entity in Luqiao District**

There are two primary LIIFCs in Luqiao District, LSAD and Taizhou Luqiao State-owned Assets Operations Co., Ltd. ("LSAO"), each with clear positioning in the development of the region. LSAO is mainly responsible for industrial investment and providing financial services in Luqiao District. LSAD is the largest infrastructure construction and state-owned assets operation entity by total assets in Luqiao District, mainly focusing on infrastructure construction and providing utility services in the area. Considering LSAD's key status in Luqiao District, we believe that the Company will not be easily replaced by other state-owned enterprises in the foreseeable future.

High sustainability of public policy businesses

As the most important infrastructure construction and state-owned assets operation entity in Luqiao District, LSAD has continuously participated in public policy businesses, such as infrastructure construction, water supply and sewage treatment, resettlement housing, grains collection and storage. There are considerable

construction projects in the pipeline, ensuring the Company's business sustainability, but also exerting high capital expenditure pressure to the Company.

Entrusted by the local government, LSAD conducts infrastructure construction projects by self-raised funds. The local government will compensate the Company with overall amounts, based on project amounts, project investments and repayment plans. As of 31 December 2023, the Company had invested RMB34.3 billion into 11 major infrastructure construction projects under construction, with an uninvested amount of RMB14.1 billion, and planned to invest RMB3.0 billion into 6 new projects. Considering uninvested amounts for projects under construction or planning, we believe the infrastructure construction business is highly sustainable, but exerting high capital expenditure pressure to the Company.

LSAD is the sole water supply and sewage treatment services provider in Luqiao District, with regional monopoly status and stable development momentum. As of 31 December 2023, the Company had one water supply plant and three pumping stations with a daily water supply capacity of 160,000 tons, and 2 sewage treatment plants with a daily sewage treatment capacity of 150,000 tons, serving around 192,200 households in Luqiao District. Due to the public welfare nature of sewage treatment services, the Company regularly receives subsidies from the local government to support its operations.

LSAD has also undertaken a number of resettlement housing projects in Luqiao District, which will be sold to the resettled households at target prices after completion. As of 31 December 2023, the Company had completed 11 resettlement housing projects, with total investment of RMB2.5 billion. Besides, the Company had 4 projects under construction, with total estimated investment of RMB2.0 billion and uninvested amount of RMB0.8 billion. As there is no project under planning at present, the sustainability of resettlement housing business is subject to uncertainty.

Entrusted by local government, LSAD also conducts the grains collection and storage functions in Luqiao District. The Company will first purchase the grains through three main stores and then store those grains in third-party factories. Given the public welfare nature of the grain business, the Company regularly receives government subsidies, which amounted to RMB23.0 million in 2023.

Medium exposure to commercial activities

LSAD's exposure to commercial activities is medium as its commercial assets accounted for less than 30% of total asset as of 31 December 2023. The commercial businesses include property development, property leasing, city operation, tourism service, hotel operation and building materials trading. We believe that the commercial risks are controllable as most of the commercial businesses generate cash flow and reasonable profit to the Company.

LSAD has continues to lease out self-owned properties in Luqiao District, such as daily necessity shopping mall, farmer's markets, cultural and sports center, fitness center, and industrial plants. The property leasing business generates stable cash flow and rental income to the Company. Benefited from rental renewal and increase in rental prices, the revenue from property leasing increased by 56.0% YoY to RMB239.3 million in 2023, with gross profit margin of 57.4%.

LSAD provides city operation services in Luqiao District through its subsidiaries, mainly involving garbage disposal and public cemetery services. The Company is responsible for more than 90% of garbage disposal in Luqiao District, and is the sole social welfare cemetery company in the area, with strong competitive advantage.

However, affected by the reduction in garbage disposal amount, total revenue from this sector decreased by 30.8% to RMB101.0 million in 2023.

LSAD conducts building materials trading through its subsidiary, with diversified products such as cement, steel and wire. The trading business depends on the demand from downstream engineering companies. In 2023, the Company's revenue from trading business increased by 28.3% YoY to RMB40.0 million.

LSAD also engages in property development business. The Company will purchase the land through open bidding, and then conduct project construction by self-raised funds. As of 31 December 2023, the Company had invested about RMB0.8 billion into two real estate project under construction, with uninvested amount of RMB1.0 billion. There is currently no project under planning. Given the downturn in China's real estate market, the property development business is subject to execution risk and destocking pressure.

The Company is also engaged in other diversified commercial businesses, such as human resources service, security service, hotel service, property management, public transportation, and tourism. However, the income scale of these businesses is small and does not contribute much to the Company's revenue and profit. Given the stable cash flow and reasonable profits from those businesses, the commercial risk is controllable.

High debt leverage and weak asset liquidity

With the continuous external financing for the construction projects, LSAD's debt burden has continued to grow over the past year, resulting in high debt leverage. The Company's total debt increased from RMB42.1 billion at end-2022 to RMB51.0 billion at end-2023, with a high total capitalization ratio of 65.8%. In addition, the Company has a relatively high short-term repayment pressure. As of 31 December 2023, its short-term debt accounted for about 35.3% of total debt. With large number of construction projects under construction, we expect that the Company will continue to rely on external financing to meet its future capital expenditure needs, and its debt leverage will remain at high level in the next 12 to 18 months.

LSAD's asset liquidity is weak, which may undermine its financial flexibility. The Company's assets mainly consist of inventories and receivables, both with low liquidity. The inventories are development costs from infrastructure construction projects, while the receivables mainly consist of uncollected payments from the local government and other state-owned enterprises, totally accounting for about 72.3% of total asset at end-2023.

Access to funding from banks and capital market

LSAD has good access to fundings, reflected by its sufficient stand-by liquidity and access to bond financing. The Company has good relationship with multiple commercial banks and policy banks in China, such as Agricultural Development Bank of China and Bank of China, and has obtained sufficient credit facilities. As of 31 December 2023, the Company's total credit facilities were RMB43.9 billion, of which the unutilized portion was RMB11.9 billion. The Company has a track record of bond issuance in the onshore debt capital market via its subsidiaries. From March 2023 to August 2024, it had issued 14 tranches of bond products such as SCPs, MTNs, and corporate bonds, raising about RMB8.6 billion, with average coupon rate of about 3%. However, LSAD has medium exposure to non-standard financing, which accounted for 21.8% of its total debts at end-2023.

Good track record of receiving government support

LSAD has a good track record of receiving support from local government in forms of capital injection, specific purpose bonds, equity transfer and financial subsidy. In 2023, the local government injected RMB1.1 billion into

the Company and provided specific purpose bonds of RMB468.4 million as support for its public policy business. Besides, the local government transferred 100% equity shares of Taizhou Luqiao Water Improvement Investment Co., Ltd to the Company. Besides, the Company received government subsidies of RMB112.8 million in 2023 to support its public policy business. Considering the important status of LSAD and its tight relationship with the local government, we expect that the support from the local government to support LSAD will continue over the next 12 to 18 months.

Medium exposure to external guarantees, with moderate contingent liability risk

LSAD has medium exposure to external guarantees. As of 31 December 2023, LSAD's external guarantees amounted to RMB5.7 billion, accounting for 21.5% of its net assets. Most of the external guarantees are provided to the state-owned enterprises in Taizhou City, with low credit risks. We believe the Company's contingent liability risk is manageable.

ESG Considerations

LSAD bears environmental risks through its infrastructure projects. Such risks could be moderated by conducting environmental studies and detailed planning before the commencement of projects and close supervision during the construction.

LSAD is also exposed to social risks as a public services provider in Luqiao District. Demographic changes, public awareness and social priorities shape government's target for LSAD, or affect the government's propensity to support the Company.

LSAD's governance considerations are also material as the Company is subject to oversight and reporting requirements to the local government, 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 \(July 2022\)](#).

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