

Credit Opinion

10 April 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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Changege Urban Construction Investment Co., Ltd.

Initial credit rating report

CCXAP assigns first-time long-term credit rating of BBB_g- to Changege Urban Construction Investment Co., Ltd., with stable outlook.

Summary

The BBB_g- long-term credit rating of Changege Urban Construction Investment Co., Ltd. (“CUCI” or the “Company”) reflects Changege City Government’s (1) 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 Changege City Government’s capacity to support reflects Changege City’s good economic fundamentals ranking top among all the counties or districts in Xuchang City with moderate fiscal metrics.

The rating also reflects the local government’s willingness to support, which is based on the Company’s (1) important role in urban construction of Changege City; and (2) track record of receiving government support.

However, the rating is constrained by the Company’s (1) increasing debt burden and moderate asset liquidity; (2) limited financing channels and standby liquidity; and (3) medium exposure to contingent liability risk.

The stable outlook on CUCI’s rating reflects our expectation that the Changege City Government’s capacity to provide support will be stable, and the Company’s characteristics such as its important position in social and economic development of Changege City will remain unchanged over the next 12 to 18 months.

Rating Drivers

- Important role in urban construction of Changge City
- Track record of receiving government support
- Increasing exposure to commercial activities
- Increasing debt burden and moderate asset liquidity
- Limited financing channels and standby bank facilities
- Medium exposure to contingent liability risk

Rating Sensitivities

What could upgrade the rating?

The rating could be upgraded if (1) Changge City 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 improved debt management or increased financing ability.

What could downgrade the rating?

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

Key Indicators

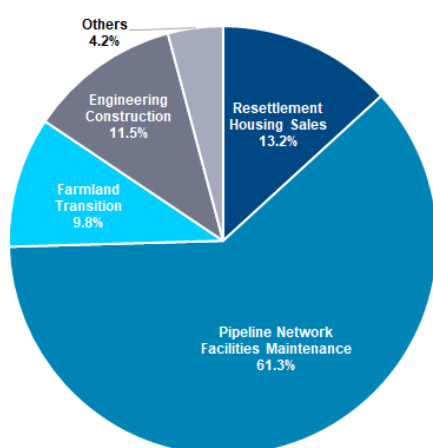
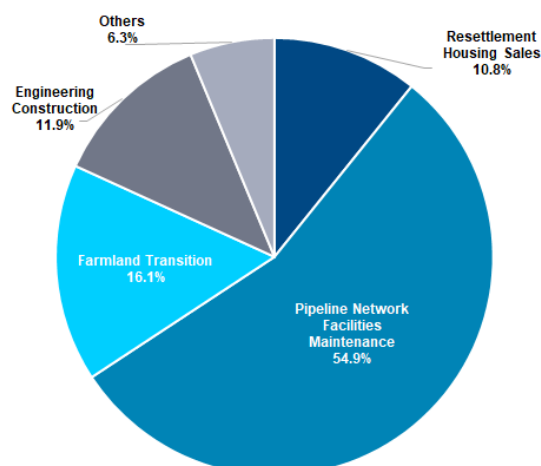
	2020FY	2021FY	2022FY	2023Q3
Total Asset (RMB billion)	3.8	4.6	9.5	9.5
Total Equity (RMB billion)	1.4	1.5	6.1	6.1
Total Revenue (RMB billion)	0.7	0.7	0.7	0.5
Total Debt/Total Capital (%)	32.3	47.7	19.9	22.4

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

Source: Company data, CCXAP research

Corporate Profile

Established in 2016, CUCI is one of the major local infrastructure investment and financing companies ("LIIFCs") in Changge City and is mainly responsible for urban construction in Changge City. CUCI is the second largest LIIFC in terms of total assets in Changge City. The Company has also diversified into other commercial business, including self-operated construction, trading, and leasing. As of 30 September 2023, the State-owned Assets Administration Commission of Change City directly owned 100% shares of the Company.

Exhibit 1. Revenue structure in 2022**Exhibit 2. Gross profit structure in 2022**

Source: Company information, CCXAP research

Rating Considerations

Government's Capacity to Provide Support

We believe that the Changge City Government has strong capacity to provide support, reflects Changge City's status as the second largest county or district by GRP in Xuchang City for years with good economic fundamentals, but is constrained by its moderate fiscal metrics.

Henan Province is located at the junction of the three major regions in China, including eastern, central and western regions. It has a strategic position as an important transportation and communication hub, and a material distribution center in China. With the good transportation and location advantages, Henan Province's GRP ranked 6th among all provinces in China in 2023.

Xuchang City is located in the central of Henan Province, which is the one of the core cities in the Central Plains Urban Agglomeration and Central Economic Zone. Xuchang City focuses on promoting six emerging industries, including new generation information technology, new materials, biopharmaceuticals, intelligent equipment, intelligent connected networks and new energy vehicles, as well as energy conservation and environmental protection industries. Supported by its industrial development, Xuchang City demonstrated steadily increasing economic strength over the past three years. In 2022, it reported a GRP of RMB374.7 billion, representing 1.8% Year-over-Year ("YoY") growth. The Xuchang Municipal Government's general budgetary revenue increased to RMB21.2 billion in 2023 from RMB18.9 billion in 2021, and tax accounted for around 66.9% of its general budgetary revenue on average over the past three years. However, Xuchang Municipal Government's fiscal balance ratio (general budgetary revenue/general budgetary expenditure) was relatively low, averaging at 59.2% over the past three years. Xuchang Municipal Government highly relied on fiscal support from higher-tier government. Moreover, the government fund revenue of Xuchang Municipal Government sharply decreased from RMB11.9 billion in 2021 to RMB6.9 billion in 2023 due to the reduction of land sales. As of end-2023, its government debt outstanding amount further increased to RMB82.8 billion from RMB67.7 billion as of end-2022.

Exhibit 3. Key economic and fiscal indicators of Xuchang City

	2021FY	2022FY	2023FY
GRP (RMB billion)	365.5	374.7	-
GRP Growth (%)	5.5	1.8	-
General Budgetary Revenue (RMB billion)	18.9	20.4	21.2
General Budgetary Expenditure (RMB billion)	32.6	34.7	34.9
Local Government Debt (RMB billion)	56.7	67.7	82.8

GRP and GRP growth in 2023 have not yet been released by Xuchang Municipal Government.

Source: Xuchang Municipal Government, CCXAP research

Changge City is a county-level city under the jurisdiction of Xuchang City and is located in the center of triangle area of Zhengzhou City, Kaifeng City, and Xuchang City, which is an important city for the integrated development of Zhengzhou City and Xuchang City. After years of development, Changge City has formed “332” industrial pattern, including 3 advantaged industries such as high-end equipment, recycled metal processing, and superhard materials and products industries, 3 distinctive industries such as packaging printing, sanitary ware, and food processing, 2 merging industries such as electronic information and biomedicine. Benefited from the location advantages and reasonable industrial structure, Changge City is the second largest county or district by GRP in Xuchang City with good economic fundamentals. From 2021 to 2023, Changge City’s GRP was RMB82.5 billion, RMB83.3 billion, RMB61.9 billion, respectively. In 2023, Changge City Government’s general budgetary revenue increased from RMB3.7 billion in 2021 to RMB4.0 billion in 2023, ranking first among all the districts or counties in Xuchang City for years. The fiscal balance of Changge City is moderate, with average fiscal balance ratio of 79.4% over the past three years. However, its government fund revenue decreased from RMB1.6 billion in 2021 to RMB396 million in 2023 due to the downturn of land market. As of 31 December 2023, the outstanding debt of Xuchang City Government was RMB9.4 billion, accounting for 15.3% of its GRP.

Exhibit 4. Key economic and fiscal indicators of Changge City

	2021FY	2022FY	2023FY
GRP (RMB billion)	82.5	83.3	61.8
GRP Growth (%)	5.3	0.7	0.1
General Budgetary Revenue (RMB billion)	3.7	3.9	4.0
General Budgetary Expenditure (RMB billion)	4.2	5.3	5.1
Local Government Debt (RMB billion)	5.8	6.8	9.4

Source: Changge City Government, CCXAP research

Government’s Willingness to Provide Support

Important role in urban construction of Changge City

CUCI is one of the major LIIFCs in Changge City and is mainly responsible for urban construction in Changge City. As the second large LIIFC by total assets, the Company plays an important role in social and economic development of Changge City, which is close to the development blueprint of local government. The Company undertakes urban construction projects through agency construction model and engineering construction model. Under agency construction model, CUCI will sign construction agreements with the entrusting parties and is responsible for overall arrangement of project fund utilization and engineering construction management. The entrusting parties would pay project payment to the construction companies through CUCI. As of 30 September 2023, the Company completed several infrastructure projects, mainly including resettlement housing, roads, landscaping, and clean heating improvement projects, with a total investment of RMB1.0 billion. Meanwhile, the

Company had 10 projects under construction, with an uninvested amount of RMB162 million. The sustainability of the Company's business is affected by the relatively small project reserves.

The Company also cooperates with some construction companies to conduct engineering construction business, mainly are local municipal infrastructure projects. CUCI would be the leader of the consortium to participate in the bidding process. As of 30 September 2023, the Company had several projects in hand with a total contract amount of around RMB130 million.

Track record of receiving government support

CUCI has track record of receiving support from the local government in the form of project payments and equity transfer to support its investments and the operation of its businesses. In 2022, the local government transferred shares of Changge Jinxiang Town Construction and Development Co., Ltd. ("CGJX") to the Company, increasing its capital reserve by RMB4.5 billion that strengthened its capital base. Most of CGJX's assets are land resources. As of 30 September 2023, CUCI has received project repayments of RMB1.9 billion in total from the local government for its urban construction, alleviating the Company's financial burden. According to the planning of the local government, CUCI is expected to receive more assets from the local government and undertake more key construction projects in Changge City in the future. Considering the Company's important role in the development of Changge City, we expect CUCI will continue receiving support from the local government.

Increasing exposure to commercial activities

CUCI participates in different commercial activities, mainly including self-operated construction. CUCI's exposure to commercial activities is relatively low, accounting for less than 15% of total assets. However, the Company has relatively large-scale of self-operated projects under planning, which may bring more capital expenditure pressure to the Company in the future.

Apart from public policy projects, CUCI also has some self-operated construction projects. As of 30 September 2023, the Company had 2 self-operated projects under construction, including one property development project and one road improvement project, with an uninvested amount of RMB335 million. At the same time, the Company had 7 self-operated projects under planning, mainly including parking lots and industrial parks, with a total investment of RMB1.8 billion. The Company expects to achieve fund balance through future sales and operation of the projects, such as leasing income and parking fees. However, the relatively large-scale of self-operated projects under planning may increase its future capital expenditure pressure and bring higher operating risk to the Company. Moreover, the investment recovery cycle of self-operated projects is long. The Company is more difficult to achieve fund balancing in short period of time.

Increasing debt burden and moderate asset liquidity

CUCI's total debt continuously increased over the past three years due to the ongoing investment for construction projects. As of 30 September 2023, the total debt increased to RMB1.8 billion from RMB675.2 million in 2020. As of 30 September 2023, its total capitalization ratio, as measured by total debt to total capital, was 22.4%, decreasing from 47.7% as of end-2021, driven by equity transfer from local government in 2022. The short-term debt accounted for around 26.9% of its total debt as of the same date. However, the cash to short-term debt ratio recorded only 0.1x, indicating certain short-term debt repayment pressure. Considering the ongoing investment for construction projects, we expect the Company would continue to rely on external financings such as bank loans, and the total debt would further increase over the next 12-18 months.

CUCI had weak asset liquidity. As of 30 September 2023, inventories, other receivables, and accounts receivables accounted for 96.2% of total assets. The inventories accounted for 60.2% of total assets, mainly including infrastructure construction, self-operated projects, and land resources transferred by local government. The receivables and other receivables were mainly receivables from the local government and other State-owned Enterprises (“SOEs”), which are considered low liquidity. Moreover, there’s a certain recovery risk from private-owned enterprises. To support the development of local private-owned enterprises, the Company provided loans to some private-owned enterprises, such as Henan Huanghe Shiye Group Co., Ltd. (“Huanghe Shiye”) and Xuchang Yong Trillion Trading Company (“XCYT”). As of 30 September 2023, the Company had loan receivables of around RMB210 million and RMB65 million from Huanghe Shiye and XCYT, respectively. Huanghe Shiye and one of its subsidiaries has been listed as a judgment debtor or a dishonest judgment debtor for multiple times. Moreover, as of 31 March 2024, Huanghe Shiye and its listed subsidiary Henan Huanghe Whirlwind Co., Ltd. had outstanding overdue payment for its commercial bills of around RMB193 million and RMB144 million, respectively. The Company has obtained properties, land, and some shares of Huanghe Shiye’s unlisted subsidiary as collateral. The Company plans to collect all the loan receivables from private-owned enterprises in 2024.

Limited financing channels and standby bank facilities

The Company mainly finances its construction projects through bank loans, accounting for around 80% of its total debts. As of 30 September 2023, the Company had obtained total bank facilities of RMB1.8 billion, the available bank facilities were only RMB470 million, indicating limited standby bank facilities. The Company had certain exposure to non-standard financing, mainly including entrusted loans from Xuchang Investment Group Co., Ltd., which then loaned to private-owned enterprises such as Huanghe Shiye and XCYT. The non-standard financing accounted for 10%-15% of the total debts as of 30 September 2024. These types of financing generally have high financing cost and short-term borrowing period, which may enlarge CUCI’s refinancing pressure.

Medium exposure to contingent liability risk

CUCI bears moderate exposure to contingent risk resulting from relatively large external guarantees. As of 30 September 2023, the Company had external guarantees of around RMB1.9 billion, accounting for 30% of its net assets, all of which were provided to local SOEs. Majority of its external guarantees was provided to Changge Jincai Public Asset Management Co., Ltd (“CGJC”). CGJC is the largest LIIFC by total assets in Change City which undertakes urban construction and investment, as well as state-owned assets operation in Changge City. The practice of mutual guarantees among local SOEs is common in Change City. In case a credit event occurs, the Company may face certain contingent liability risks and cross-default risks.

ESG Considerations

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

CUCI bears social risks as it implements public policy initiatives by building public infrastructure in Change City. Demographic changes, public awareness and social priorities shape the Company’s development targets and ultimately affect the local government’s propensity to support the Company.

CUCI's governance considerations are also material as the Company is subject to oversight by local government and has to meet several reporting requirements, reflecting its public-policy role and status as a government-owned entity.

Structural considerations

CUCI's senior unsecured debt rating is equal to its long-term credit rating. We believe that government support will flow through the Company given its important position in social and economic development of Changge City, 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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