

Credit Opinion

25 June 2024

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

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Zhaoqing Gaoyao District State-Owned Assets Operation Co., Ltd.

Surveillance credit rating report

CCXAP affirms Zhaoqing Gaoyao District State-Owned Assets Operation Co., Ltd.'s long-term credit rating of BBB_g-, with stable outlook.

Summary

The BBB_g- long-term credit rating of Zhaoqing Gaoyao District State-Owned Assets Operation Co., Ltd. ("GSAO" or the "Company") reflects the Gaoyao District Government's (1) strong capacity to provide support, and (2) very high willingness to provide support to the Company, based on our assessment of the Company's characteristics.

Our assessment of the Gaoyao District Government's capacity to provide support reflects its leading economic status in Zhaoqing City, with economic growth potential and stable fiscal profile.

The rating also reflects the local government's willingness to provide support, which is based on the Company's (1) important position in infrastructure construction and water supply of Gaoyao District; (2) good track record of receiving governmental payments; and (3) reasonable debt leverage.

However, the Company's rating is constrained by the Company's (1) high short-term debt repayment pressure; (2) moderate access to funding with high reliance on non-standard fundings; and (3) medium contingent liability risk from external debt guarantees.

The stable outlook on GSAO's rating reflects our expectation that the local government's capacity to provide support will remain stable, and that the Company will maintain its important position of infrastructure construction and water supply in Gaoyao District and continue to receive ongoing government support.

Rating Drivers

- Important position in infrastructure construction and water supply of Gaoyao District
- Good track record of receiving governmental payments
- Medium exposure to commercial activities, with manageable commercial risks
- Reasonable debt leverage but with high short-term debt repayment pressure
- Moderate access to funding with high reliance on non-standard fundings
- Medium contingent liability risk from external debt guarantees

Rating Sensitivities

What could upgrade the rating?

The rating could be upgraded if (1) the local government's ability to provide support strengthens; and (2) the Company's characteristics change in a way that strengthens local government's willingness to provide support, such as improvement in access to funding and asset quality.

What could downgrade the rating?

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

Key Indicators

	2021FY	2022FY	2023FY
Total Asset (RMB billion)	18.7	22.4	27.8
Total Equity (RMB billion)	9.9	11.4	11.9
Total Revenue (RMB billion)	1.0	2.0	2.0
Total Debt/Total Capital (%)	34.4	36.3	39.4

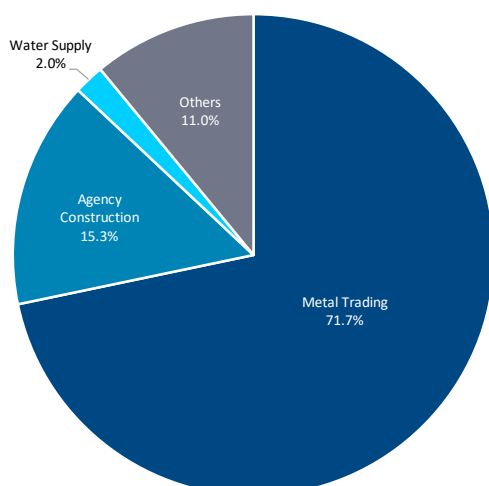
All ratios and figures are calculated using CCXAP's adjustments.

Source: Company data, CCXAP research

Corporate Profile

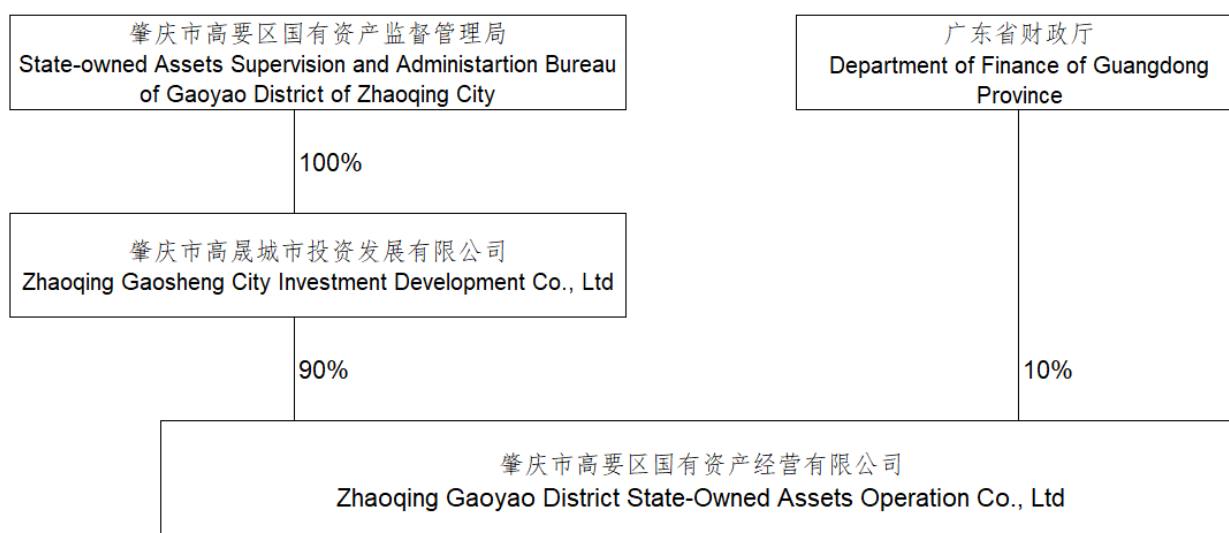
Founded in 1994, GSAO is a key state-owned enterprise in Gaoyao District of Zhaoqing City. The Company is mainly engaged in public policy businesses such as infrastructure construction and water supply, and commercial businesses such as metal trading, sale of civil explosives, provision of security services, property leasing, engineering construction and self-operated projects construction. In November 2022, under the approval of the Gaoyao District government, the 90% of equity interests of the Company were transferred to Zhaoqing Gaosheng Urban Investment Development Co., Ltd. ("GSUI") from the State-owned Assets Supervision and Administration Bureau of Gaoyao District of Zhaoqing City ("Gaoyao SASAB"), who still was the ultimate controlling shareholder of the Company, holding 90% of the Company's equity interests through GSUI, while the Department of Finance of Guangdong Province held the remaining 10% as of 31 December 2023.

Exhibit 1. GSAO's revenue structure in 2023



Source: Company information, CCXAP research

Exhibit 2. Shareholding Chart as of 31 December 2023



Source: Company information, CCXAP research

Rating Considerations

Government's Capacity to Provide Support

We believe that the Gaoyao District Government has strong capacity to provide support, given its leading economic status in Zhaoqing City, with economic growth potential and stable fiscal profile.

Guangdong Province is one of the most economically developed provinces in China, and its comprehensive economic strength outperforms other provinces. Thanks to industrial production and consumption recovery after the epidemic, the gross regional product ("GRP") of Guangdong Province achieved RMB13.6 trillion in 2023, ranking first among all provinces in China, with a year-on-year ("YoY") increase of 4.8%. In 2023, its general budgetary revenue reached RMB1.4 trillion, ranking first in China for more than 30 consecutive years.

Located in the western part of Guangdong Province, Zhaoqing City is the largest inland city in the Guangdong

Hong Kong-Macao Greater Bay Area (“Greater Bay Area”). Zhaoqing City has a well-developed transportation network, forming a comprehensive transportation hub with "one intercity railway, two express links, seven expressways, and one golden waterway". In recent years, Zhaoqing City has developed three industrial clusters valued over RMB100 billion, namely new energy vehicles, advanced equipment manufacturing, and energy conservation and environmental protection. Benefiting from the ongoing development of agriculture and manufacturing industries, the GRP of Zhaoqing City increased by 3.7% YoY to RMB279.3 billion in 2023, ranking 12th among 21 cities in Guangdong Province. Zhaoqing Municipal Government's fiscal strength also improved along with the economic growth, its general budgetary revenue had increased from RMB14.6 billion in 2021 to RMB17.7 billion in 2023, of which tax income accounted for 50.6% on average during the period. However, the fiscal balance of Zhaoqing City is still weak, averaging at 39.9% from 2021 to 2023. Zhaoqing City's local government had an increasing debt burden as its outstanding debt balance was RMB113.3 billion at end-2023 compared to RMB99.6 billion at end-2022, accounting for 40.6% of GRP.

Exhibit 3. Key Economic and Fiscal Indicators of Zhaoqing City

	2021FY	2022FY	2023FY
GRP (RMB billion)	265.0	270.5	279.3
GRP Growth (%)	10.5	1.1	3.7
General Budgetary Revenue (RMB billion)	14.7	16.1	17.7
General Budgetary Expenditure (RMB billion)	39.7	39.7	41.8
Local Government Debt (RMB billion)	87.7	99.6	113.3

Source: Statistics Bureau of Zhaoqing City, CCXAP research

Gaoyao District is located in the central part of Guangdong Province, belonging to the Pearl River Delta, Guangzhou-Foshan-Zhaoqing Economic Circle and Zhaoqing Economic Development Center. Gaoyao District has a relatively good investment potential, ranking 39th by investment potential among Top 100 districts in China according to the research results of High-quality Development Index of China's Small- and Medium-sized Cities in 2023. It is also one of the top five counties in terms of comprehensive economic development counties in Guangdong. Gaoyao District has formed an industrial layout with auto parts and hardware processing industries as the core industries, supplemented by advanced equipment manufacturing, chemical industry and health and leisure industries. With the good location advantages and industrial layout, Gaoyao District's economic strength improved steadily with the GRP increased 4.5% YoY to RMB56.2 billion in 2023, ranking first among all districts in Zhaoqing City. Due to a substantially increase in non-tax revenue generated from sale of mineral resources, Gaoyao District Government's general budgetary revenue grew rapidly to RMB3.4 billion in 2023, representing a 20.3% YoY growth rate. Moreover, its fiscal balance ratio was at an average of 52.2% from 2021 to 2023, which was at a modest level. Gaoyao District Government has a manageable debt profile as the outstanding debt balance of Gaoyao District Government was RMB11.1 billion at end-2023, accounting for 19.7% of GRP.

Exhibit 4. Key Economic and Fiscal Indicators of Gaoyao District

	2021FY	2022FY	2023FY
GRP (RMB billion)	50.7	54.2	56.2
GRP Growth (%)	11.5	3.5	4.5
General Budgetary Revenue (RMB billion)	2.2	2.8	3.4
General Budgetary Expenditure (RMB billion)	5.2	5.4	5.5
Local Government Debt (RMB billion)	7.6	8.9	11.1

Source: Statistics Bureau of Gaoyao District, CCXAP research

Government's Willingness to Provide Support

Important position in infrastructure construction and water supply of Gaoyao District

Apart from the Company, there are other three main LIIFCs in Gaoyao District, which are GSUI, Zhaoqing Gaoyao Jiantou Investment and Development Group Co., Ltd. ("GJID") and Zhaoqing Gaoyao District Hengyao Investment Development Co., Ltd ("GYHY"), each with clear positioning in the infrastructure development of Gaoyao District. GSUI is the largest and the most important infrastructure construction and state-owned asset operation entity in the region, owning the shares in the other three LIIFCs in Gaoyao District. GJID is primarily responsible for the infrastructure construction in the new urban area of Gaoyao District and Jinli High-tech Zone, while GSAO is mainly responsible for the operation of state-owned assets as well as the infrastructure construction in the old urban area of Gaoyao District. GYHY is mainly responsible for road and transportation infrastructure construction and other commercial business including hardware commodity trading and state-owned asset leasing. GSAO plays an important strategic role in supporting and promoting the urbanization and industrialization of Gaoyao District. We believe that GSAO's important role in the development of Gaoyao District and its public welfare functions are unlikely to be replaced in the short-to-medium term.

GSAO continued to conduct infrastructure construction projects under agency construction model. As of 31 December 2023, the Company had completed 2 key infrastructure construction projects with a total invested amount of RMB979.1 million and a recognized repayment of RMB619.3 million. Meanwhile, the Company had 4 infrastructure construction projects under construction with a total planned investment of RMB3.4 billion and an uninvested amount of RMB1.7 billion. The Company also has received project repayment for its these projects of RMB2.1 billion. Although the future investment amount is relatively large, funds from special government bonds can alleviate part of the capital expenditure pressure. However, there is no agency project under planning as the Company is switching its business focus from agency infrastructure construction to self-built construction. The sustainability of agency construction business is subject to uncertainty.

GSAO's water supply business is conducted by its subsidiary. It provides residential and industrial water supply to local residents and enterprises, as well as installation of water supply facilities. This business has a regional dominant position as it covers the main area of Gaoyao District, except for Dawan town and Jinli town. In 2023, the Company distributed water of over 60 million tons to 118,300 households in Gaoyao District via five water plants and pipe network of 263 kilometers. The water supply service will cover the whole Gaoyao District when construction completion of a new water plant, which can further enhance its market position and revenue generation. In 2023, the Company achieved a revenue of RMB41.0 million from the water supply business, but accounting for only 2.0% of its total revenue. We expect the water supply business will continue to provide stable income to the Company but is constrained by its relatively small scale.

Medium exposure to commercial activities, with manageable commercial risks

We consider GSAO have medium exposure to commercial activities, such as metal trading, sale of civil explosives, provision of security services, meat processing, sale of fuel gas, driving training, property leasing, engineering construction and self-operated projects construction, accounting for around 20% to 25% of its total assets at end-2023. Nonetheless, we expect that the overall commercial risk is manageable, as its subsidiary, namely Zhaoqing Gaoyao District Materials Co., Ltd., which was mainly responsible for sale of civil explosives and sale of fuel gas businesses and participated in property leasing and engineering construction businesses, was transferred out in the progress of restructuring of state-owned enterprises in Gaoyao District in March 2024.

The Company has participated in self-operated projects construction, including industrial park construction, pipe network expansion, and land reclamation, and plans to achieve fund balancing through projects operations and

leasing. As of 31 December 2023, the Company had 7 self-operated projects under construction, with a total planned investment of RMB1.7 billion and an uninvested amount of about RMB368.4 million. Meanwhile, the Company had 4 self-operated projects under planning, including photovoltaic, smart parking, gas stations, and farmers' market upgrades projects, with a total estimated investment of RMB3.0 billion, indicating certain investment pressure. Although these self-operated projects could be a good supplement to the Company's revenue, they may bring certain operational uncertainties and financial risks to the Company.

GSAO has started metal trading business since 2021, which became the largest income contributor to the Company, accounted for 71.7% of its total revenue in 2023, with trading products mainly including electrolytic copper and aluminum ingot. However, the profitability of the business is low as recorded a gross profit margin of less than 1% in 2023. Moreover, the metal trading business is subject to concentration risks due to its relatively high reliance on top 5 customers and suppliers, accounting for 68.3% and 100% of the total sales and total procurements in 2023.

GSAO also undertakes engineering construction projects through bidding in public market. In virtue of a new entity transferred in, the profitability of the engineering construction business has improved, as reflected by its gross profit margin of 11.0% in 2023. However, the contribution of engineering construction business to the Company's overall gross profit is constrained by its small scale since the revenue generated from engineering construction business was RMB798.7 million, representing only 3.9% of its total revenue.

GSAO is also engaged in several market-oriented businesses, including sale of civil explosives, provision of security services, meat processing, sale of fuel gas, property leasing and driving training businesses. However, the income scale of these businesses is small, totaling RMB143.3 million and accounting for 7.1% of its total revenue in 2023, with limited contribution to the Company's revenue.

Good track record of receiving government payments

GSAO has a good track record of receiving ongoing government payments, in the form of operating subsidies, capital injections, project payments, and high-quality asset transfers. Since 2020, the Gaoyao SASAB has injected monetary capital of RMB1.6 billion and transferred assets including forest assets, commercial properties, factory assets and intangible assets to the Company without compensation, increasing capital reserves by RMB4.1 billion in total, substantially enhancing GSAO's capital strength. The Company also regularly receives government subsidies and project repayments from the local government over the past three years. From 2021 to 2023, the Company received government subsidies of RMB793.0 million and project repayments of RMB952.2 million to support its operation and project construction. Additionally, Gaoyao SASAB plans to further transfer assets to the Company, and will also provide operational subsidies to support the Company's growth and expansion in line with its business needs. Given its important strategic position in Gaoyao District, we expect the local government will provide ongoing and stable support to the Company.

Reasonable debt leverage but with high short-term debt repayment pressure

The Company has maintained moderate debt leverage. As of end-2023, the Company's total debt increased 19.2% YoY from RMB6.5 billion in 2022 to RMB7.8 billion in 2023 while the total capitalization ratio rose from 36.2% to 39.4% during the same period, which is reasonable. However, the Company is exposed to debt repayment pressure due to its large short-term debt maturities. As of 31 December 2023, its short-term debt accounted for around 54.4% of total debt. Meanwhile, after excluding restricted cash, the cash to short-term debt ratio was 0.1x, indicating large debt refinancing needs. Given the Company's future capital expenditure

pressure for its investment and construction projects, we expect the Company will continue to rely on external financing to meet its future capital expenditures and its debt leverage will increase in the next 12 to 18 months.

Moderate asset liquidity

GSAO's asset liquidity is moderate as its assets mainly consist of total receivables and inventories, both with low liquidity. As of 31 December 2023, the Company's total receivables and inventories accounted for 66.7% of total assets. The Company's inventories are mainly land use rights and infrastructure construction costs, and the total receivables are mainly unreceived project payments from Gaoyao SASAB and other local state-owned investment or construction companies. However, the Company's investment properties can provide small amount of supplementary income and cash flow. As of 31 December 2023, the Company had investment properties of RMB2.0 billion, accounting for 7.2% of total assets.

In addition, as of 31 December 2023, the Company's restricted assets amounted to RMB1.8 billion, representing around 6.4% of its total assets, consisting mainly of monetary capital, long-term equity investments and receivables, which may undermine the Company's financing flexibility.

Moderate access to funding with high reliance on non-standard fundings

GSAO shows moderate access to funding, as it mainly relies on bank loans and non-standard financing, which may increase its refinancing risk. As of 31 December 2023, the Company's non-standard debts accounted for about 45.1% of its total debt. The non-standard financing products consist of trusts and financial leasing, which generally have high financing cost, bringing higher refinancing pressure to the Company. However, we believe the Company's refinancing risk can be partially alleviated by its sufficient standby liquidity. As of 31 December 2023, the Company had total credit facilities of RMB7.2 billion, with unutilized portion of RMB2.9 billion. In 2021, it raised USD48 million via the offshore bond market, with a coupon rate of 1.9%. We expect the Company will continue to broaden its financing channels by increasing credit facilities and issuing onshore bonds and improve debt structure by reducing the proportion of non-standard debts.

Medium contingent liability risk from external debt guarantees

GSAO has significant external guarantee exposures related to local SOEs, which could potentially increase its repayment obligations. As of 31 December 2023, the Company had outstanding external guarantees of RMB5.2 billion, accounting for 43.6% of its net assets. All the external guarantees are provided to local state-owned enterprises in Gaoyao District, mostly to GJID, as mutual guarantees between local SOEs are common in the region. Considering that most of these local SOEs are expected to be supported by the local government when necessary, we believe contingent risk would be controllable.

ESG Considerations

GSAO faces environmental risks because it has undertaken infrastructure development projects. 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.

GSAO bears social risks as it implements public policy initiatives by undertaking infrastructure construction projects in Gaoyao District. Demographic changes, public awareness and social priorities shape the Company's development targets and ultimately affect the local government's willingness to support the Company.

GSAO's governance considerations are also material as the Company is subject to oversight by the Gaoyao

District Government and has to meet several reporting requirements, 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 \(July 2022\)](#).

Appendix

Exhibit 5. Peer Comparison in 2023

	Zhaoqing Gaoyao District State-Owned Assets Operation Co., Ltd.	Zhaoqing Gaoyao Jiantou Investment and Development Group Co., Ltd.
Long-Term Credit Rating	BBB _g -	BBB _g -
Shareholder	Zhaoqing Gaosheng Urban Investment Development Co., Ltd (90%); Department of Finance of Guangdong Province (10%)	Zhaoqing Gaosheng Urban Investment Development Co., Ltd
Positioning	Responsible for engineering project construction including development of parks, infrastructure construction, and shantytown reconstruction in old urban area of Gaoyao District.	Responsible for urban public infrastructure construction; civil engineering construction and landscaping engineering construction in new town of Gaoyao District and Jinli High-tech Zone.
Total Asset (RMB billion)	27.8	21.9
Total Equity (RMB billion)	11.9	8.9
Total Revenue (RMB billion)	2.0	2.2
Total Debt/Total Capital (%)	39.4	54.1

All ratios and figures are calculated using CCXAP's adjustments.
Source: Company data, CCXAP research

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