

Chengdu Wenjiang Xingrongxi City Operation Group Co., Ltd.

Initial Issuer Report

Summary

Issuer Rating	BBB-
Outlook	Stable
Location	China
Industry	Local Government
	Financing Vehicle
Date	7 March 2022

Lianhe Ratings Global Limited (“Lianhe Global”) has assigned ‘BBB-’ global scale Long-term Issuer Credit Rating to Chengdu Wenjiang Xingrongxi City Operation Group Co., Ltd. (“WXCO”). The Outlook is Stable.

Summary

The Issuer Credit Rating reflects a high possibility that Wenjiang District People’s Government of Chengdu (“Wenjiang government”) would provide strong support to WXCO if needed, in light of its 100% ownership of WXCO, WXCO’s strategic position as the major development and operation entity of Wenjiang District in Chengdu and the strong linkage between the Wenjiang government and WXCO including management supervision, strategic alignment, and ongoing operational and financial support. In addition, the Wenjiang government may face significant negative impact on its reputation and financing activities should WXCO encounter any operational or financial difficulties.

The Stable Outlook reflects our expectation that WXCO’s strategic importance would remain intact while the Wenjiang government will continue to ensure WXCO’s stable operation.

Rating Rationale

Wenjiang Government’s Full Ownership: The Wenjiang government has 100% ownership of WXCO via the State-owned Assets Supervision and Administration Bureau of Wenjiang District (“Wenjiang SASAB”), which is appointed by the government to supervise state-owned entities. WXCO was established in April 2016, with an initial registered capital of RMB1 million. The registered capital of WXCO increased to RMB2 billion in 2020. The increase in registered capital will be injected in the form of cash and/or physical assets by the Wenjiang SASAB in three years. WXCO’s paid-in capital was RMB131 million at end-September 2021.

High Strategic Importance: WXCO is the largest and major LGFV responsible for infrastructure construction and operation, as well as resettlement housing construction and sales in Wenjiang. WXCO is the main urban operation comprehensive service provider in Wenjiang, and it has undertaken the construction of most infrastructure projects, such as municipal road and bridge construction, tunnel construction and relocation, and pipe network reconstruction projects in the region. Meanwhile, WXCO is also involved in building materials sales under franchise arrangement, leasing business and asset management business, with a diversified industrial structure, to support the urban development in Wenjiang.

Government Supervision and Strategic Alignment: The Wenjiang government has strong control and supervision over WXCO, including the control of the board of directors, senior management appointments, and major strategic, investment and financing planning. WXCO’s business operation and development have been aligned with the government’s economic and social policies in Wenjiang. In addition, the Wenjiang government has an assessment system on WXCO. The Wenjiang SASAB and the Finance Bureau of Wenjiang District will assign auditor to audit WXCO’s financial and operating data on a periodic basis.

Ongoing Government Support: WXCO has received support from the government such as subsidies, capital injections and financial support. The Wenjiang government and Finance Bureau of Wenjiang District have also repurchased a considerable amount of the

Key Figures of Wenjiang and WXCO (RMB billion)

	2019	2020
Wenjiang		
GDP	59.6	62.4
GDP growth rate (%)	8.1	5.1
Budgetary revenue	4.5	4.6
Government fund	5.0	7.4
Transfer payment	1.3	2.1
Budgetary expenditure	5.7	7.1
WXCO		
Assets	58.7	66.6
Equity	36.3	38.5
Revenue	2.2	2.9

Source: Wenjiang government, Finance Bureau of Wenjiang, WXCO and Lianhe Global’s calculations

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Applicable Criteria

China Local Government Financing Vehicle Criteria (31 December 2021)



completed infrastructure projects from WXCO in the past few years. WXCO is expected to continue receiving repayment from the government in the future from the projects completed and projects under development.

Moderate Financials and Liquidity Position: WXCO's earnings generation capability has been weak given its focus on contracting construction. WXCO's financial leverage (total liabilities to assets) was moderate at 43.5% at end-September 2021. Apart from the financial support from the government, WXCO has access to financing channels such as bank loans, bond issuance and other financing channels to support its debt repayment and business operation. WXCO had a total outstanding debt of RMB19.5 billion at end-2021, while the short-term debt was RMB4.7 billion, compared with its available credit lines of RMB15.7 billion at the same time.

Moderate Economy and Fiscal Strength Underpin Wenjiang: With GDP growth rate of 8.1% and 5.1% in 2019 and 2020, respectively, Wenjiang's economic growth had been mainly fueled by the secondary and tertiary industries in the past few years. The service industry had become the main GDP growth driver with the tertiary industry (the service sector) accounting for the largest, at 58.9%, of Wenjiang's GDP in 2020, followed by the secondary industry's (comprising manufacturing and construction) 34.7%.

Wenjiang's aggregate fiscal revenue was mainly derived from the stable budgetary revenue with tax revenue accounting for c. 80% in the past three years, followed by sustained growth in government-managed fund income. Wenjiang's fiscal debt ratio (total government debt outstanding/aggregate revenue) is slightly higher than the average level in Chengdu. Wenjiang's government debt increased from RMB11.3 billion at end-2019 to RMB14.4 billion at end-2020, representing an increase of c. 27%, mainly due to the new special bonds for municipal projects.

Rating Sensitivities

We would consider downgrading WXCO's rating if (1) there is perceived weakening in support from the Wenjiang government, particularly due to its reduced strategic importance with diminished government functions, or (2) there is a significant reduction of the Wenjiang government's ownership of WXCO, or (3) there is a downgrade in our internal credit assessment on the Wenjiang government.

We would consider upgrading WXCO's rating if (1) there is strengthened support from the Wenjiang government, or (2) there is an upgrade in our internal credit assessment on the Wenjiang government.

Operating Environment

Stable Economy with Sustained Growth of Wenjiang District

Wenjiang District, a municipal district under the administration of Chengdu, is the sub-center district in the west of Chengdu and 16 kilometers away from the urban area. In recent years, Wenjiang has made continuous progress in urban and rural infrastructure construction such as transportation, energy, and municipal public facilities, and has completed a transportation network and now has a better connection with the main urban area of Chengdu. Wenjiang has a total land area of 277 square kilometers, and a residential population of c. 0.97 million with an urbanization rate of 78.0%, according to the 7th National Census in 2020.

Wenjiang realized RMB59.6 billion GDP in 2019 and RMB62.4 billion in 2020, representing a year-over-year growth rate of 8.1% and 5.1%, respectively. Wenjiang's economic growth is mainly fueled by the secondary and tertiary industries in the past few years, among which the proportion of the secondary industry has dropped to less than 40% since 2019. These two industry segments realized added value of RMB23.3 billion and RMB36.7 billion in 2020, respectively. Wenjiang's whole-year GDP amount was ranked 10th in Chengdu in 2020 (out of 20 county-level cities and districts). GDP per capita was c. RMB64,500 at end-2020.

Wenjiang's GDP and Fixed Asset Investment

(RMB billion)	2018	2019	2020
GDP	54.5	59.6	62.4
-Primary industry (%)	3.5	3.7	3.7
-Secondary industry (%)	49.8	36.7	34.7
-Tertiary industry (%)	46.7	59.6	58.9
GDP growth rate (%)	8.8	8.1	5.1
Fixed asset investment	4.4	4.9	5.3
Fixed asset investment growth rate (%)	6.3	11.3	8.3
Population (million)	0.5	0.6	1.0

Source: Wenjiang government's website and Lianhe Global's calculation

Moderate Fiscal Condition of Wenjiang District

Wenjiang's fiscal revenue remained stable at around RMB4.6 billion in 2020, with a modest growth in the past two years. Its budgetary revenue grew by 11.1%, 9.8% and 2.2% in 2018, 2019 and 2020, respectively. The tax revenue as a percentage of budgetary revenue accounted for c. 80% in the past three years. The revenue from government-managed fund was mainly from the transfer of land use right, which increased by 54.6% in 2020 compared to that in 2019, leading the government-managed fund to increase by about 39.5% to c. RMB7.4 billion in 2020. Wenjiang's financial self-sufficiency rate is insufficient, thus it continues to receive subsidies from the higher government.

Wenjiang's fiscal debt ratio (total government debt outstanding / aggregate revenue) is relatively high compared with other county-level cities or districts within Chengdu. Wenjiang's government debt increased from RMB11.3 billion at end-2019 to RMB14.4 billion at end-2020, representing an increase of c. 27%, mainly due to the new special bonds for municipal projects.

Wenjiang's Fiscal Condition (RMB billion)	2018	2019	2020
Budgetary revenue	4.1	4.5	4.6
Budgetary revenue growth rate (%)	10.1	11.0	2.4
Tax revenue	3.2	3.6	3.7
Tax revenue (% of budgetary revenue)	79.8	79.5	80.2
Government fund income	4.1	5.0	7.4
Transfer payment	1.2	1.3	2.1
Aggregate revenue	9.4	10.9	14.1
Budgetary expenditure	5.7	5.7	7.1
Budget deficit ¹ (%)	-39.0	-26.7	-54.3

¹ Budget deficit = (1-budgetary expenditure / budgetary revenue) * 100%

Source: Finance Bureau of Wenjiang District and Lianhe Global's calculations

Ownership Structure and Profile

Full State Ownership with Strong Government Supervision

WXCO was established under the approval of Chengdu Wenjiang State-owned Assets and Finance Office with an initial registered capital of RMB1 million in April 2016. In May 2016, 100% equity of three state-owned entities, 成都温江区国投兴城投资有限公司 ("国投兴城"), 成都新城西城市投资经营中心 ("新城西") and 成都铸康实业有限公司 ("铸康实业") were transferred to WXCO free of charge under the Document No.10 [2016] issued by the Wenjiang government. In 2019, the ultimate controlling shareholder of WXCO was changed to Chengdu Wenjiang State-owned Assets Supervision and Administration Bureau ("Wenjiang SASAB") and the registered capital was increased to RMB2 billion in February and December, respectively. The increase in registered capital will be injected in the form of cash and/or physical assets by the Wenjiang SASAB in three years, according to the Wenjiang SASAB. In 2020, the Wenjiang SASAB increased the capital of RMB130 million in the form of cash to WXCO, and the paid-in capital of WXCO increased to RMB131 million at end-2020. The Wenjiang SASAB was the only shareholder with 100% ownership of WXCO and the Wenjiang government is its ultimate controller at end-2021.

Strategic Importance and Government Linkage

Strategic Importance of WXCO to Wenjiang District in Chengdu

WXCO is the biggest and one of the most important LGFVs responsible for infrastructure construction and operation in Wenjiang. WXCO is the main urban operation comprehensive service provider in Wenjiang, and it has undertaken the construction of most infrastructure projects, such as municipal road and bridge construction, tunnel construction and relocation, and pipe network reconstruction projects in the region. Meanwhile, WXCO is also involved in building materials sales, leasing business and asset management business, with a diversified industrial structure. We believe that the Wenjiang government is willing to extend support to WXCO in view of its strategic important role as one of the most important developers of Wenjiang District to support the local economic and urban development.

Strong Linkage with the Wenjiang Government

WXCO's linkage with the local government is strong as it is wholly owned by the Wenjiang government through the Wenjiang SASAB. The Wenjiang government holds 100% stake in WXCO and it is the ultimate shareholder.

The Wenjiang government has strong control and supervision over WXCO, including control of the board of directors, senior management appointments, and major strategic, investment and financing planning. WXCO's strategic planning and development have been aligned with the local government's economic and social policies, aiming to develop Wenjiang District. In addition, the Wenjiang government has an assessment system on WXCO. The Wenjiang SASAB and the Finance Bureau of Wenjiang District will assign auditor to audit WXCO's financial and operating data on a periodic basis.

Ongoing Government Support

WXCO has received supports from the local government for its business operation, which are not limited to capital injection, subsidies, allocation of land resources or assets and guidance from the government. WXCO increased its registered capital to RMB2 billion in 2020. The increase in registered capital will be injected in the form of cash and/or physical assets by the Wenjiang SASAB in three years.

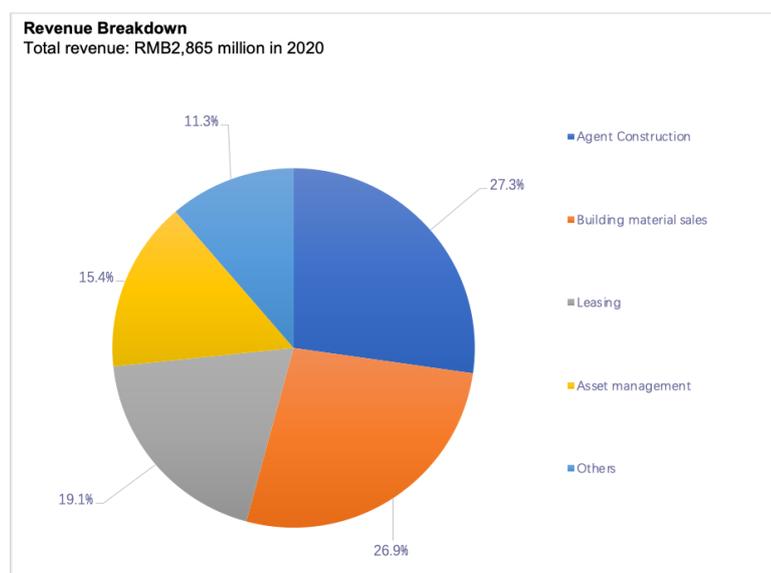
WXCO has received financial subsidies from the local government mainly for supporting projects related to public infrastructure or special projects, although the amount is minimal. WXCO received a total of c. RMB9.3 million of government subsidies between 2018 and nine months ended September 2021. We believe WXCO will likely continue to receive timely government support in the form of operational and/or financial subsidies.

Business Profile

The Flagship LGFV Responsible for Infrastructure Construction and Operation of Wenjiang District in Chengdu

WXCO is the biggest and one of the most important LGFVs responsible for infrastructure construction and investment in Wenjiang, with total assets of RMB66.6 billion at end-2020 and RMB70.0 billion at end-September 2021. WXCO is the main urban operation comprehensive service provider in Wenjiang, and it has undertaken the construction of most major infrastructure projects, such as municipal road and bridge construction, tunnel construction and relocation, and pipe network reconstruction projects in the region.

Meanwhile, WXCO is also involved in building materials sales, leasing business and asset management business, with a diversified industrial structure. The total revenue of WXCO was c. RMB2,651 million, RMB2,246 million, RMB2,865 million and RMB1,710 million in 2018, 2019, 2020 and nine months ended September 2021, respectively. In view of business income structure, agent construction business, leasing business, building materials sales business and asset management business are the main sources of income of WXCO.



Source: WXCO's annual report and Lianhe Global's calculation

Infrastructure Construction and Resettlement Housing Construction

The infrastructure construction and resettlement housing construction business is mainly operated by its subsidiaries, 国投兴城, 新城西 and 铸康实业. This business segment adopts the agent construction agreement mode, and the entrusting party is mainly Finance Bureau of Wenjiang District, the Wenjiang government and other LGfVs in Wenjiang. After the construction is completed, the entrusting party will buy back the project, according to the provisions, which usually includes the investment amount (including financing cost) plus a percentage of management fee (normally 15% for infrastructure construction projects, and 9% for resettlement construction projects) as the final settlement amount upon completion.

WXCO had 29 completed infrastructure construction projects, 11 projects under development and 7 proposed projects at end-June 2021, which are mainly municipal roads, schools and other comprehensive renovation projects. Meanwhile, WXCO also had 9 completed resettlement projects and 6 projects under development. In addition, WXCO also obtained the approval of a national project, Wenjiang Wenmiao Area Urban Renewal Planning Project. The projects under development and proposed projects will put pressure on its capital expenditure.

Building Materials Sales

WXCO is responsible for the sales of sand, gravel and concrete in Wenjiang. It began to expand the trading business of concrete sales in 2018. The business model is to purchase finished concrete from social concrete sellers and sell it to other state-owned enterprises in the region. With the approval from the government, WXCO has the sand mining franchise of sand and gravel resources in the relevant regions. The sales revenue of building materials has been growing in the past few years, with revenue of RMB451.4 million, RMB519.9 million and RMB772.1 million, accounting for c. 17.0%, 23.1% and 27.0% of WXCO's total revenue in 2018, 2019 and 2020, respectively. The gross profit margin for the building materials sales segment is at around 23%, which is higher than the agent construction business.

The inventory balance of this segment is relatively low, due to the high turnover business model and the strong demand from downstream customers, as well as WXCO's intention to decrease the management cost and inventory cost. However, due to seasonal factors, the sand and stone mining volume has decreased since the beginning of 2021, while the strong demand downstream remained the same. Thus, the inventory level went through a further decrease.

Leasing

WXCO leases the resettlement house and pipe network to Construction Bureau of Wenjiang District, Wenjiang District Municipal Public Utilities Bureau, Wenjiang District Education Bureau and Chengdu Wenjiang District Water Supply Company, and receives the corresponding rental income. WXCO also leases its own shops, dust suppression vehicles and other assets to other units to obtain rental income. The rental fees are usually paid annually or semiannually. The revenue from this business segment was RMB469.0 million, RMB470.4 million and RMB548.6 million, accounting for c. 17.7%, 20.9% and 19.2% of total revenue in 2018, 2019 and 2020, respectively. The gross margin for this segment was around 50%, which is significantly higher than that of other segments.

Asset Management

The asset management business mainly refers to WXCO's management and maintenance services for some roads and other transportation infrastructure in Wenjiang. The main leased assets are roads and other transportation infrastructure owned by WXCO. WXCO's revenue from the asset management business was RMB331.9 million, RMB422.3 million and RMB440.1 million, accounting for c.12.5%, 18.8% and 15.4% of total revenue in 2018, 2019 and 2020, respectively. The main asset management contracts signed by WXCO will expire at end-June 2026 at the earliest, and the rest will expire from 2029 to 2031.

Other Businesses

Other businesses include resettlement sales and sewage treatment business in Wenjiang. In addition, according to the Wenjiang government's integration plan, WXCO will be responsible for the operation of parking lots in Wenjiang, which will increase its income from the transportation sector.

Financial Profile

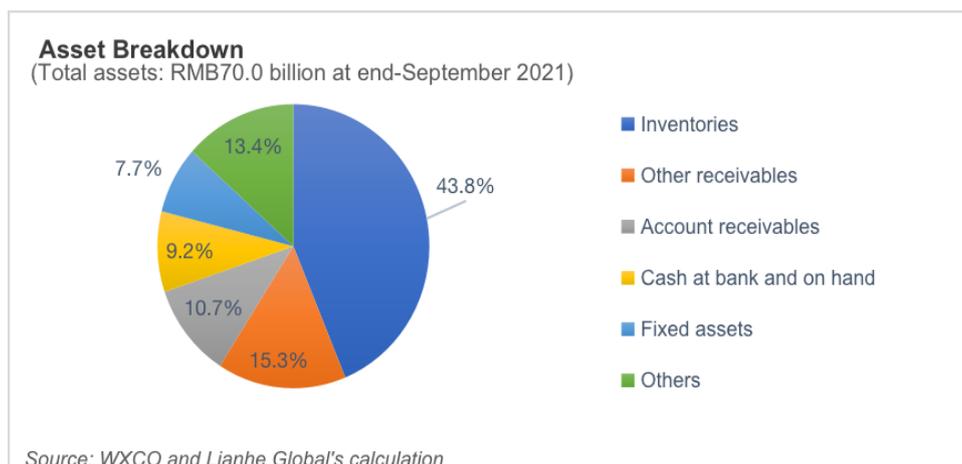
Balance Sheet Structure and Quality

Balance Sheet Structure and Quality				
(RMB million)	2018	2019	2020	3Q2021
Total Asset	41,643	58,683	66,592	70,038
Equity	22,688	36,349	38,474	39,598
Debt	13,747	18,530	24,194	25,256
Debt / (Debt + Equity) (%)	37.7	33.8	38.6	38.9
LT Debt	10,688	13,415	17,364	18,196
LT Debt / (LT Debt + Equity) (%)	32.0	27.0	31.1	31.5

Source: WXCO's financial reports, WXCO and Lianhe Global's calculations

WXCO's total assets showed a continuous growth trend in the past few years, with growth rate of 40.9%, 13.5% and 5.2% at end-2019, end-2020 and nine months ended September 2021, respectively. The asset increase in 2021 was mainly due to the increase in inventories

and cash. The asset structure was stable, which mainly consisted of inventories (43.8%), other receivables (15.3%), account receivables (10.7%) and cash (9.2%) at end-September 2021. Other receivables reached RMB10.7 billion at end-September 2021, accounting for c. 19.3% of the current assets, and the amount from the government, mainly the Finance Bureau of Wenjiang District, accounted for a large amount. Per WXCO, the government has a plan to settle the receivables with stable payments per annum lowering the risk to become bad debts. The inventories reached RMB30.7 billion at end-September 2021, accounting for c. 55.3% of the current assets. It mainly included land to be developed and development cost.



WXCO's financial leverage (total liabilities to assets) increased to 43.5% at end-September 2021, representing an increase of 1.3% compared with that at end-2020. The total liabilities increased by 8.3% to RMB30.4 billion, while the total equities increased by 2.9% to RMB39.6 billion and the equity structure remained largely unchanged at the same time. Total debt increased to RMB25.3 billion at end-September 2021, representing an increase of 4.4% compared with that at end-2020, and was mainly caused by the issuance of long-term bonds. Debt over capitalization ratio was 38.9% at end-September 2021. WXCO relies mainly on external financing to support its capital expenditure. The capital expenditure of WXCO will likely increase, given the number of projects to be developed.

Cash Flow

Cash Flow (RMB million)	2018	2019	2020	9M2021
Cash Inflows from Operation	1,132	1,921	2,004	5,560
Cash Outflows from Operation	1,553	1,715	3,027	4,377
Net CF from Operation	-421	205	-1,023	1,182
Cash Inflows from Investment	1,646	301	764	749
Cash Outflows from Investment	14	64	2,049	267
Net CF from Investment	1,632	236	-1,285	482
Cash Inflows from Financing	4,212	8,952	10,738	7,439
Capital Contribution	-	-	130	-
Borrowings	2,843	7,915	9,794	6,634
Others	1,368	1,037	814	805
Cash Outflows from Financing	5,556	7,638	6,667	7,218
Net CF from Financing	-1,344	1,314	4,071	221
Net Increase in Cash and cash equivalent	-133	1,756	1,763	1,887

Source: WXCO's financial reports

Debt Servicing Capability

At end-2021, WXCO had a total credit line of RMB38.5 billion, of which approximately RMB15.7 billion was available, compared with its debt to be due within one year of RMB4,717.8 million. WXCO has access to multiple financing channels including bank borrowings, bond issuance and other financing channels such as trust loan and finance lease etc. Bank loans accounted for c. 49% of while bonds and non-traditional financings accounted for c. 37% and c. 14% of total debt, respectively, at end-2021.

Debt Maturity Profile at end-2021

(RMB million)	Amount	Percentage
1Q2022	499.0	2.6%
2Q2022	2,002.5	10.3%
3Q2022	829.7	4.3%
4Q2022	1,386.6	7.1%
2023	1,642.7	8.4%
2024	3,927.0	20.1%
2025	2,400.0	12.3%
2026 and thereafter	6,811.2	34.9%
Total	19,498.7	100.0%

Source: WXCO and Lianhe Global's calculations

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