

Zhengzhou Urban Construction Investment Group Co., Ltd.

Surveillance Report

Summary

Issuer Rating	A-
Outlook	Stable
Location	China
Industry	Local Government
Financing Vehicle	
Date	14 July 2022

Lianhe Ratings Global Limited (“Lianhe Global”) has affirmed ‘A-’ global scale Long-term Issuer and Issuance Credit Rating of Zhengzhou Urban Construction Investment Group Co., Ltd. (“ZCC”). Issuer Rating Outlook Stable.

Summary

The Issuer Credit Rating reflects a high possibility that Henan’s Zhengzhou municipal government would provide strong support to ZCC if needed. This mainly considers the Zhengzhou municipal government’s full ownership of ZCC, the high strategic importance of ZCC to Zhengzhou in the municipal infrastructure construction and maintenance, and the strong linkage between the Zhengzhou municipal government and ZCC, including management supervision, strategic alignment, and ongoing operational and financial support. In addition, the Zhengzhou municipal government may face significant negative impact on its reputation and business and financing activities should ZCC encounter any operational or financial difficulties.

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

Rating Rationale

Zhengzhou Government’s Full Ownership: The Zhengzhou municipal government has 100% ownership of ZCC via the State-owned Assets Supervision and Administration Commission of Zhengzhou (“Zhengzhou SASAC”) which is appointed by the government to supervise state-owned entities. Zhengzhou SASAC is the only shareholder of ZCC through its fully-owned Zhengzhou Real Estate Group Co., Ltd.

High Strategic Importance: ZCC is one of Zhengzhou’s major investment and financing platforms and has undertaken various businesses including municipal infrastructure construction and maintenance, hotel operations and commodity trading to support the economic development in Zhengzhou. ZCC has extended its infrastructure project scope from roads and bridges to shantytown renovation, public service facilities, and ecological and environmental governance.

Government Supervision and Strategic Alignment: The Zhengzhou municipal government and Zhengzhou SASAC have strong control and supervision over ZCC, including control of the board of directors and the supervisory committee, senior management appointments, and major strategic, investment and financing planning. ZCC’s business operation and development have been aligned with the government’s economic and social policies. As one of the national central cities in the central region of China, Zhengzhou has devoted to optimise its economic structure and strengthen the transportation connections and logistic services to promote urban and rural development.

Ongoing Government Support: ZCC has received capital and asset injections from the Zhengzhou government and related government entities. The injections include road maintenance right and municipal infrastructure such as roads and bridges. The Zhengzhou

Key Figures of Zhengzhou and ZCC

(RMB billion)	2020	2021
Zhengzhou		
GDP	1,200.3	1,269.1
GDP growth rate (%)	3.0	4.7
Budgetary revenue	125.9	122.4
Government fund	105.9	89.6
Transfer payment	44.3	44.3 ¹
Budgetary expenditure	172.1	162.4
ZCC		
Assets	44.1	47.6
Equity	18.5	19.0
Revenue	1.1	1.2

¹ Transfer payment in 2021 is estimated given the lack of such information

Source: Zhengzhou Bureau of Statistics, Zhengzhou Finance Bureau, ZCC and Lianhe Global’s calculations

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Applicable Criteria

China Local Government Financing Vehicle Criteria (31 December 2021)

Finance Bureau has also supported ZZC's operations through various forms of cooperation, such as government procurement of services and public-private partnership projects.

The Flood and the Recrudescence of COVID-19 Cases Put Pressure on Zhengzhou's Economy and Fiscal Strength: Ongoing economic development, industrialization and urbanization have supported Zhengzhou's high GDP growth rate in the past few years. However, the flood and the recrudescence of COVID-19 cases in 2H2021 significantly slowed down Zhengzhou's economic growth. Specifically, Zhengzhou recorded a GDP growth rate of 4.7% in 2021, compared with 6.3% in Henan province and 8.1% in China. Moreover, Zhengzhou recorded a decrease of 6.2% in fixed asset investment in 2021, mainly due to the slowdown in property investment and infrastructure investment.

Zhengzhou's aggregate fiscal revenues are mainly derived from the stable budgetary revenue and government fund income. Zhengzhou's budgetary revenue is relatively stable, with tax revenue accounting for 68-75% of it during 2018-2021. However, Zhengzhou's government fund income is more volatile, mainly due to the COVID-19 cases in 2020-2021, and the flood in 2021 as well. Subsidies from higher government authorities have been relatively small. Remaining relatively stable at 60-70% during 2017-2019, Zhengzhou's debt ratio (i.e. total government debt divided by aggregate revenue) increased to c. 79% in 2020 and bumped up to c. 97% in 2021, mainly due to the sharp decline in government fund income and the increase in government debts. Nevertheless, the trend of increasing budget deficit reversed with drops in both 2020 and 2021, because of the continuous decline in budgetary expenditure in 2020-2021.

Moderately Weak Financial Matrix: ZZC's profitability has been weak given its focus on public projects with limited commercial-oriented activities. The reliance on debt financing to support its capital expenditure drove up ZZC's financial leverage (total liabilities to assets) to 60.5% at end-March 2022 from 50.9% at end-2018, which was mitigated by its sufficient liquidity with cash on hand and standby credit facilities. As of end-March 2022, ZZC had RMB7.3 billion of outstanding debt due within one year, compared with its unrestricted cash of RMB6.0 billion, unused onshore and offshore bond quota of RMB307 million and USD350 million, respectively, and undrawn credit facilities of RMB16.3 billion.

Rating Sensitivities

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

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

Company Profile

ZZC was established as a fully stated-owned entity in December 2007 under the No. 136 [2007] of the Zhengzhou Municipal People's Government with an initial capital of RMB10 million. ZZC's registered capital was increased to RMB1 billion at end-March 2022. Zhengzhou SASAC is the only shareholder with 100% ownership through its fully-owned Zhengzhou Real Estate Group Co., Ltd. (郑州地产集团有限公司) and the Zhengzhou municipal government is the ultimate controller.

ZZC had a number of wholly-owned or controlled subsidiaries that were consolidated into its financial statements at end-2021, with operations across various industries, including public infrastructure construction and maintenance, hotel operations and trading businesses. As one of the major state-owned asset management and infrastructure investment and operation entity in Zhengzhou, ZZC has played an important role for the economic development of Zhengzhou, and has received ongoing support from the Zhengzhou municipal government in terms of asset transfer, capital injection and financial subsidies.

ZZC is mainly responsible for the construction and investment of municipal infrastructure projects such as urban roads and bridges within the Fourth Ring of Zhengzhou City. Major completed projects include the first phase of Beijing-Guangzhou Expressway Project, Jinshui Road West Extension Project, East Third Ring Expressway Project, etc. ZZC has further expanded its project scope to shantytown renovation, public service facilities, and ecological and environmental governance. Major projects currently under construction include Zhengzhou Grand Theatre, Zhengzhou Citizen Activity Centre, Jialu River Ecological Greening Project, and Zhongyuan New District Shantytown Renovation.

Full List of Issuance Ratings

A full list of affirmed issuance ratings is included below. Any rating action on ZZC's rating would result in a similar rating action on the USD notes:

- USD300 million 3.8% senior unsecured bonds due 2022
- USD200 million 3.8% senior unsecured bonds due 2025

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