

# Shaoxing City Investment Group Limited

## Surveillance Report

### Summary

Issuer Rating	A
Outlook	Stable
Location	China
Industry	Local Government Financing Vehicle
Date	12 August 2022

Lianhe Ratings Global Limited ("Lianhe Global") has upgraded the global scale Long-term Issuer and Issuance Credit Rating of Shaoxing City Investment Group Limited ("SCIG" or "the company") to 'A' from 'A-'. Issuer Rating Outlook is Stable.

### Summary

The Issuer Credit Rating upgrade reflects an upgrade in our internal credit assessment on Zhejiang's Shaoxing Municipal Government and the expectation of a continuing of a high possibility that the Shaoxing Municipal Government would provide strong support to SCIG if needed. This mainly considers the Shaoxing Municipal Government's 90% ownership of SCIG (with the other 10% owned by Zhejiang Finance Development Co., Ltd., a wholly owned entity of the Zhejiang Provincial Department of Finance, to subsidize the Provincial Social Security Fund), the high importance of SCIG to Shaoxing in the utilities (gas and water) infrastructures and services, as well as urban infrastructure and social-housing construction area, and the strong linkage between the Shaoxing Municipal Government and SCIG, including management supervision, ongoing operational and financial support. In addition, the Shaoxing Municipal Government may face significant negative impact on its reputation and financing activities if SCIG encounters any operational and financial difficulties.

Lianhe Global has also upgraded the global scale Long-term Issuance Credit Rating of the senior unsecured USD bonds issued by SCIG to 'A' from 'A-' at the same time. A full list of Issuance Rating is included in this report.

The Stable Outlook reflects our expectation that SCIG's strategic importance would remain intact while the Shaoxing Municipal Government will continue to ensure SCIG's stable operation.

### Rating Rationale

**Strong Linkage with the Shaoxing Municipal Government:** The Shaoxing Municipal Government, via Shaoxing State-owned Assets Supervision and Administration Commission (SASAC), holds 90% of SCIG, while the remaining 10% of SCIG's shares were owned by Zhejiang Finance Development Co., Ltd., a wholly owned entity of Zhejiang Provincial Department of Finance, to subsidize the provincial Social Security Fund.

**High Strategic Importance:** SCIG remains Shaoxing's major operating entity of urban infrastructures and social-housing. It is responsible for the key projects' construction in Shaoxing, including National Highway 329 and Provincial Highway S308's renovations, as well as Shaoxing Chinese medicine hospital and Shaoxing University's expansion projects. SCIG also is the only natural gas infrastructure and services provider in the urban area of Shaoxing.

**Government Supervision and Strategic Alignment:** The Shaoxing Municipal Government is the ultimate shareholder of SCIG and has strong control and supervision over SCIG, including the decision on its strategic development plan and supervision of its major funding decisions. In addition, Shaoxing SASAC reviews the audit report of the

### Key Figures of Shaoxing and SCIG

(RMB billion)	2020	2021
<b>Shaoxing</b>		
GDP	600.1	679.5
GDP growth rate (%)	3.3	8.7
Budgetary revenue	54.3	60.4
Government fund	83.4	115.5
Transfer payment	7.4	7.0
Budgetary expenditure	66.7	71.5
<b>SCIG</b>		
Assets	54.5	65.3
Equity	22.7	25.8
Revenue	7.4	9.4

Source: Shaoxing Bureau of Statistics, Shaoxing Finance Bureau, SCIG and Lianhe Global's calculations

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### Applicable Criteria

China Local Government Financing Vehicle Criteria (31 December 2021)

operation of SCIG by an external auditor. SCIG's business operation and development have been aligned with the government's economic and social policies.

**Ongoing Government Support:** SCIG received continuous financial support from the Shaoxing Municipal Government in the past three years, amounting to RMB2,781 million, RMB1,522 million and RMB4,698 million, respectively. These subsidies were to support the maintenance of completed infrastructure projects held by SCIG as well as the launch of key projects. At the same time, the government injected some fixed assets such as properties and transferred the equities of other SOEs to SCIG to expand the company's asset base.

**Moderate Standalone Financials:** SCIG realized total revenue of c. RMB9.4 billion, representing a year-on-year growth rate of 27.2% in 2021. Gas sales remains the largest revenue source. However, the company's gross margin declined to 12.4% from 13.7%, mainly due to the rising gas procurement cost.

SCIG's financial leverage (total liabilities to assets) increased to 62.5% at end-March 2022 from 58.3% at end-2020. This was to support its investment in infrastructures. The company's infrastructure construction segment generated sizeable fixed assets and construction in progress, amounting to c. RMB20.1 billion and c. RMB12.0 billion, which accounted for 29.2% and 17.3% of its total assets at end-March 2022.

We believe that these assets lack liquidity under SCIG's current business model. The fixed assets mainly consisted of completed not-for-profit roads and bridges, while the construction in progress mainly consisted of such infrastructure projects being developed. SCIG usually holds these projects on its balance sheet upon completion to earn management fees and operating subsidies.

**Improving Debt Maturity Profile:** SCIG's short-term debt/total debt ratio reduced to 25% at end-March 2022 from 34% at end-2020. It had c. RMB8.2 billion of cash (including restricted cash of RMB33.9 million) against its short-term debt of c. RMB8.1 billion at end-March 2022. In addition, SCIG has access to multiple financing channels, including bank loans, syndicated loans and bond issuances, etc., to support its debt repayment and business operation.

**Relatively Strong Economic and Fiscal Condition of Shaoxing:** Shaoxing's GDP reached RMB679.5 billion in 2021, representing a moderately high growth rate of 8.7%. However, its two years' average GDP growth rate for 2020 and 2021 was 6%, which was lower than the pre-Covid years' growth of 7.1% and 7.0% in 2018 and 2019, respectively. Nevertheless, Shaoxing's economic development level is above the average level of Zhejiang Province. Its GDP size was ranked 4<sup>th</sup> among 11 prefecture-level cities, and its GDP per capita (RMB127,875) was higher than that of Zhejiang Province (RMB113,032) in 2021.

Shaoxing's aggregate fiscal revenue was mainly derived from its budgetary revenue and government fund income, while the contribution of transfer payment received was small as Shaoxing is a relatively developed city. Shaoxing realized budgetary revenue of c. RMB60.4 billion in 2021, representing a year-on-year growth rate of 11.1%. The tax revenue accounted for c. 80% of its budget revenue in the past three years. Shaoxing's budget deficit was manageable. The deficit rate decreased to 11.8% in 2021 from 21.3% in 2019 because its budgetary revenue grew continuously, while the Shaoxing Municipal Government managed to reduce unnecessary expenditures and administrative expenses. Shaoxing's government fund income increased rapidly in the past three years. It reached c. RMB115.5 billion in 2021, up from c. RMB 71.6 billion in 2019. Land sales contributed more than 90% of the government fund income. The growth may slow down amid China's property market downturn. At end-2021, Shaoxing's total outstanding debt increased by 15.1% to c.

RMB143.7 billion (including special debt of c. RMB98.9 billion) from c. RMB124.8 billion (including special debt of c. RMB61.9 billion) at end-2020.

### Rating Sensitivities

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

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

### Company Profile

SCIG was established as a wholly state-owned entity in 1999 with an initial capital of RMB220 million. From 1999 to 2020, the company's registered capital had been increased multiple times to RMB3,300 million, including but not limited to capital and asset injection and equity transfer from the local governments and related departments. According to the decision of the Shaoxing SASAC, it transferred 10% of SCIG's equity free of charge to Zhejiang Finance Development Co., Ltd. (浙江省财务开发有限责任公司) in September 2020, which is a wholly-owned company of the Zhejiang Provincial Department of Finance (浙江省财政厅). Consequently, Shaoxing SASAC holds 90% equity of SCIG and the Shaoxing Municipal Government is the ultimate controller.

SCIG is one of the important state-owned LGFVs under the Shaoxing Municipal Government. Its business mainly focuses on the municipal urban infrastructure construction, utilities (gas and water supply), social housing and is supplemented by merchandise sales, such as building materials and electrical equipment.

### Full List of Issuance Rating

A full list of affirmed Issuance rating is included below. Any rating action on SCIG's rating would result in a similar rating action on the USD bonds:

- USD 700 million 2.5% senior unsecured bonds due 2026 upgraded to 'A' from 'A-'

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