Shuifa Group Co., Ltd.

Surveillance Report

Summary	
Issuer Rating	A
Outlook	Stable
Location	China
Industry	Local Investment and Development Companies
Date	21 December 2022

Key Figures of Shandong and Shuifa

(RMB billion)	2020	2021
Shandong		
GDP	7,312.9	8,309.6
GDP growth rate (%)	3.6	8.3
Budgetary revenue	656.0	728.5
Government fund	727.9	797.7
Transfer payment	363.2	326.2
Budgetary expenditure	1,253.2	1,171.3
Shuifa		
Assets	141.8	168.0
Equity	31.4	38.3
Revenue	45.2	77.0

Source: Shandong Bureau of Statistics, the Shandong government, Shuifa and Lianhe Global's calculations

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Applicable Criteria
China Local Investment and Development Companies Criteria (5 December 2022)

Lianhe Global has affirmed 'A' global scale Long-term Issuer Credit Rating of Shuifa Group Co., Ltd. ("Shuifa"); Rating Outlook Stable

Summary

The Issuer Credit Rating reflects our internal assessment on the Shandong provincial government ("Shandong government"), and the gradual shift of Shuifa's development focus to business outside Shandong province as well as the increasing contributions from certain commercial segments. All in all, we believe there is still a high possibility that the Shandong government would provide moderately strong support to Shuifa if needed, in light of its majority ownership of Shuifa, Shuifa's strategic position as the sole provincial level, and the major water supply and water-related project development platform in Shandong Province and the strong linkage between the Shandong government and Shuifa including management supervision, strategic alignment, and ongoing operational and financial support. In addition, the Shandong government may face negative impact on its reputation and business and financing activities should Shuifa encounter any operational or financial difficulties.

The Stable Outlook reflects our expectation that Shuifa's business profile will remain intact while the Shandong government will continue to ensure Shuifa's stable operation.

Rating Rationale

Local Government's Ownership and Supervision: At end-September 2022, the State-owned Assets Supervision and Administration of Shandong Province ("Shandong SASAC") held 70% stake in Shuifa while Shandong Guo Hui Investment Co., Ltd. and Shandong Social Security Fund Council held 20% and 10%, respectively. Shuifa's linkage with the local government is strong as it is majority-owned by the Shandong government. The controlling shareholder and actual controller is the Shandong SASAC under the Shandong government. The registered and paid-in capital were both RMB5.2 billion at end-September 2022.

Strategic Importance and Alignment: Shuifa is still the largest provincial level LIDC platform for water supply and water-related development projects with a dominant market position in Shandong province, as well as the largest raw water supplier in Shandong province. Despite the fact that Shuifa's role is hard to replace in a short period of time considering its expertise, size and project under construction, it has increasing contributions from certain commercial segments in clean energy, modern agriculture, real estate development, etc., which would constrain its strategic position in Shandong vis-à-vis traditional LIDCs that focus on providing public goods and services.

In addition, Shuifa has gradually diversified its development focus to business outside Shandong province, such as clean energy business in Jilin province, modern agriculture business in Xinjiang Uygur Autonomous and water-related, hydroelectric power plants constructions in Gansu province etc., which may have a potential impact on Shuifa's strategic importance in Shandong province.

Strong Government Supervision and Strategic Alignment: The Shandong government has strong control and supervision over Shuifa, including control of the board of directors and the supervisory committee, and approvals of senior manager appointments and major operating and financing plans. Shuifa's strategic planning and development have been aligned with the provincial government's economic and national policies. In addition, the government assigns auditors to audit Shuifa's financial and operating data on a periodic basis.

Ongoing Government Support: Shuifa continued to receive capital and assets injections from the Shandong government. The injections included capital, cash and other tangible/intangible assets. Shuifa received assets injections of approximately RMB1.9 billion in 2021 in the form of grass field operation right. Shuifa consistently received financial subsidies from the local government mainly for supporting projects related to public infrastructure or special projects and enjoys a series of tax policy benefits. Shuifa received RMB276.0 million and RMB86.7 million of government subsidies and tax benefits in 2021 and for the first half of 2022, respectively, which decreased moderately compared to that in 2018-2020 as a result of its diminishing hydraulic engineering construction and water supply projects. Shuifa's increasing proportion of self-operating business, increasingly diversified projects distribution outside the Shandong province, as well as the increasing risk exposure to different local financial subsidy policies, may have a potential impact on the stability of the financial subsidies received from the Shandong government.

Moderately Weak Standalone Profile: Shuifa's financial leverage (total liabilities to assets) was 76.2% at end-September 2022, slightly decreased from 77.2% at end-2021. Shuifa mainly relies on external financing to support its capital expenditure. In view of its projects under construction and development, we expect Shuifa's capital expenditure needs to continue. Shuifa had a cash balance of approximately RMB9.2 billion (unrestricted cash of RMB4.3 billion) and unused credit line of c. RMB49.8 billion at end-September 2022, compared with its debt will be due within one year of c. RMB30.5 billion at the same time. Besides, Shuifa has access to various financing channels including bank loans, onshore and offshore bonds issuance, other non-traditional financing such as finance leasing and trust loan.

Economy and Fiscal Strength Underpin Shandong: Shandong's GDP increased to RMB8,309 billion, representing a year-over-year growth rate of 8.3%, ranked third in China. Its economic growth was mainly fuelled by the secondary and tertiary industries. Shandong's fiscal strength maintained steady growth in 2021. Its budgetary revenue and government-managed fund revenue grew by c. 11% and 9.6%, respectively, in 2021. The debt ratio (i.e. total government debt divided by aggregate fiscal revenue) of local government increased to c. 107% at end-2021 from c. 70.8% at end-2020, while the budget deficit of improved to -60.7% in 2021 as a result of decreasing budgetary expenditures.

Rating Sensitivities

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

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

Company Profile

Shuifa Group Co., Ltd. was founded in 2009 and registered with the Shandong Market Supervision and Administration Bureau. Its headquarters are in Jinan City, Shandong Province. As of end-September 2022, Shuifa's registered capital and paid-in capital were both RMB5.206

billion. The SASAC of Shandong Province, Shandong Guo Hui Investment Co., Ltd. and Shandong Social Security Fund Council held 70%, 20% and 10% of the company's shares, respectively, at end-September 2022. The controlling shareholder and actual controller is SASAC of Shandong Province.

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