

Wuxi Urban Construction Development Group Co., Ltd.

Initial Issuer Report

Summary

Issuer Rating	A+
Outlook	Stable
Location	China
Industry	Local Investment and Development Companies
Date	11 January 2023

Lianhe Ratings Global Limited (“Lianhe Global”) has assigned ‘A+’ global scale Long-term Issuer Credit Rating with Stable Outlook to Wuxi Urban Construction Development Group Co., Ltd. (“WUCD” or “the company”)

Summary

The Issuer Credit Rating reflects a high possibility that the Wuxi Municipal People's Government (“Wuxi government”) would provide strong support to WUCD if needed, in light of its full ownership of WUCD, WUCD's strategic position as an important Local Investment and Development Company (“LIDC”) for urban construction and development in Wuxi and the strong linkage between the Wuxi government and WUCD including management supervision, strategic alignment, and ongoing operational and financial support. In addition, the Wuxi government may face significant negative impact on its reputation and business and financing activities should WUCD encounters any operational or financial difficulties.

The Stable Outlook reflects our expectation that WUCD's strategic importance would remain intact while the Wuxi government will continue to ensure WUCD's stable operation.

Rating Rationale

Wuxi Government's Ownership and Supervision: WUCD is wholly owned by the Wuxi government through State-owned Assets Supervision and Administration Committee of Wuxi government (“Wuxi SASAC”). The Wuxi government has strong control and supervision over WUCD, including control of the board of directors, management supervision, decision on its strategic development and investment plan, supervision of its major funding decisions and daily operation, etc.

Strategic Importance and Strategic Alignment: As an important LIDC directly under the Wuxi government, WUCD is mainly responsible for urban and rural construction, affordable housing construction and other functions in the region. WUCD undertakes various urban and rural construction projects in Wuxi, such as hospital, school, agent construction projects and other important city-level urban renewal and rural revitalization projects, etc. WUCD's strategic planning and development have been aligned with the local government's economic and social policies. It carries out the directions and policies of affordable housing construction of the Wuxi government to support the local economy growth.

Ongoing Government Support: WUCD has received supports from the local government for its business operation, which are not limited to capital injections, government subsidies, allocation of equity or assets and guidance from the government in its daily management. In addition, WUCD has received financial subsidies from the local government mainly for supporting business development. The company received a total of c. RMB19.48 million of government subsidies between 2019 and 2021. We believe WUCD is likely going to receive government support in the form of operational and/or financial subsidies in the future.

Financials and Liquidity of WUCD: The reorganization of WUCD, mainly the deconsolidation of Wuxi Taihu New City Development Group Co., Ltd. (“TNCG”), led to changes on its asset structure. WUCD's total assets decreased by c. 47% from RMB123.3 billion at end-2021 to RMB65.3 billion at end-September 2022. Nevertheless, WUCD's

Key Figures of Wuxi and WUCD

(RMB billion)	2020	2021
Wuxi		
GDP	1,237.0	1,400.3
GDP growth rate (%)	3.7	8.8
Budgetary revenue	107.6	120.0
Government fund	98.8	122.6
Transfer payment	18.0	15.2
Budgetary expenditure	121.5	135.8
WUCD		
Assets	106.7	123.3
Equity	36.9	42.2
Revenue	3.6	4.7

Source: Public information, WUCD and Lianhe Global's calculations

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Applicable Criteria

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

financial leverage improved. Its leverage ratio, measured as total liabilities over total assets, improved to 44.2% at end-September 2022 from 65.8% at end-2021, while the total debt capitalization ratio declined to 33.6% at end-September 2022 from 58.6% at end-2021. The liquidity of WUCD was relatively adequate. At end-September 2022, WUCD had a cash balance of c. RMB5.7 billion (restricted cash was approximately RMB0.1 billion) and a total credit line of RMB36.3 billion, of which approximately RMB26.3 billion was available, compared with its debt to be due within one year of c. RMB5.5 billion. WUCD has access to multiple financing channels including bank borrowings, corporate bonds and other financing channels such as trust loan and finance lease etc.

Economic and Fiscal Conditions of Wuxi: As a prefecture-level city in Jiangsu Province, Wuxi is one of the fifteen national economic center cities and one of the central cities in Yangtze River Delta. Wuxi realized a GDP of RMB1,400.3 billion in 2021, which ranked 3rd in Jiangsu Province. Besides, Wuxi's GDP per capita was c. RMB187 thousand in 2021, ranking 3rd among all prefecture-level cities in China. The Wuxi government's budgetary revenues recorded a constant growth with increasing growth rates in the past three years, which were 2.4%, 3.8% and 11.6% in 2019, 2020 and 2021, respectively. Its budget deficit was manageable, with relatively low deficit rates of -7.8%, -13.0% and -13.1% in 2019, 2020 and 2021, respectively. In addition, the Wuxi government's debt ratio, as measured by total government debt/aggregate revenue, was maintained at a moderate level of c.60% in the past 3 years.

Rating Sensitivities

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

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

Operating Environment

Economic Condition of Wuxi

Wuxi is a prefecture-level city in Jiangsu Province. It is one of the fifteen national economic center cities and one of the central cities in Yangtze River Delta. Meanwhile, Wuxi is a major transportation hub in East China, and has formed a three-dimensional transportation network composed of railway, highway, waterway and aviation. Wuxi administers over 5 districts and 2 county-level cities with a total land area of 4,627 square kilometers with a residential population of c. 7.5 million. The urbanization rate reached 82.9% at end-2021.

Wuxi's economy is well developed. It realized a GDP of RMB1,400.3 billion in 2021, which ranked 3rd (behind Suzhou and Nanjing) in Jiangsu Province. Besides, Wuxi's GDP per capita was c. RMB187 thousand in 2021, ranking 3rd (behind Erdos and Karamay but ahead of Beijing) among all prefecture-level cities in China.

Wuxi picked up its GDP growth momentum in 2021 with a high growth rate of 8.8%, up from 3.7% in 2020. The economic growth was mainly fueled by the secondary and tertiary industries, accounting for 47.9% and 51.2% of its aggregate GDP, respectively, while the share of the primary sector was minimum (0.9%) in 2021. However, the city's fixed asset investment growth slowed to 4.5% in 2021 from 6.1% in 2019 and 2020.

Wuxi's GDP and Fixed Asset Investment

(RMB billion)	2019	2020	2021
GDP	1,185.2	1,237.0	1,400.3
-Primary industry (%)	1.0	1.0	0.9
-Secondary industry (%)	47.5	46.5	47.9
-Tertiary industry (%)	51.5	52.5	51.2
GDP growth rate (%)	6.7	3.7	8.8
Fixed asset investment	359.6	381.5	398.5
Fixed asset investment growth rate (%)	6.1	6.1	4.5
Population (million)	6.6	7.5	7.5

Source: Public information and Lianhe Global's calculations

Fiscal Condition of Wuxi

The Wuxi government's budgetary revenues recorded a constant growth with increasing growth rates in the past three years, which were 2.4%, 3.8% and 11.6% in 2019, 2020 and 2021, respectively. The budgetary revenue increased to RMB120.0 billion in 2021 from 103.6 billion in 2019. Over the same period, the tax revenue's contribution stood at above 80% level. In addition, the government-managed fund income has grown significantly to RMB122.6 billion in 2021, up from RMB79.7 billion in 2019, representing a high compound annual growth rate ("CAGR") of c. 24%.

The Wuxi government received relatively small transfer payments from higher governments, given its relatively strong fiscal conditions. Its budget deficit was manageable, with relatively low deficit rates of -7.8%, -13.0% and -13.1% in 2019, 2020 and 2021, respectively. In addition, the Wuxi government's debt ratio, as measured by total government debt/aggregate revenue, was maintained at a moderate level of c.60% in the past 3 years.

Wuxi's Fiscal Condition			
(RMB billion)	2019	2020	2021
Budgetary revenue	103.6	107.6	120.0
Budgetary revenue growth rate (%)	2.4	3.8	11.6
Tax revenue	87.0	88.9	98.4
Tax revenue (% of budgetary revenue)	84.0	82.7	82.0
Government fund income	79.7	98.8	122.6
Transfer payment	11.7	18.0	15.2
Aggregate revenue	199.3	226.2	162.6
Budgetary expenditure	111.8	121.5	135.8
Budget deficit ¹ (%)	-7.8	-13.0	-13.1

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

Source: Finance Bureau of Wuxi and Lianhe Global's calculations

Ownership Structure and Profile

Government's Ownership and Supervision

WUCD (former name: Wuxi City Development Group Co., Ltd.) was established as a wholly LIDC under the approval of Document No. 121 [2008] issued by the Wuxi government, with an initial registered capital of RMB50 million on 26th May 2008. WUCD received multiple times capital injections in the form of cash or equity transfer from the Wuxi government after establishment. In December 2020, the shareholder of WUCD changed from the Wuxi government to Wuxi SASAC. At end-September 2022, WUCD's registered capital and paid-in capital were approximately RMB11.9 billion and the Wuxi SASAC was the only shareholder with 100% ownership of WUCD.

To optimize the structure of state-owned entities in Wuxi, WUCD went through a major restructuring with other LIDC in January 2022. According to the resolution of the board of directors of Wuxi Construction and Development Investment Co., Ltd. ("WCDI"), WCDI no longer entrusts WUCD with its voting rights of TNCG. The shares of TNCG held by WUCD and WCDI remained unchanged, that were 31.2% and 17.06%, respectively. As a result, TNCG was no longer consolidated into the scope of WUCD's consolidated financial statements. In addition, the Wuxi government decided to transfer 49% shares of WCDI and 26% shares of Wuxi Environmental Protection Group Co., Ltd. ("WEPG") to WUCD. After the restructuring, WUCD holds 34.57% shares (including 3.37% of indirect holdings) of TNCG as a long-term equity investment.

Since this reorganization was under the requirement of the local government, we expect that it will not have adverse effect on WUCD's daily operation or management except the consolidated financial reports.

Strategic Importance and Government Linkage

Strategic Importance of WUCD to Wuxi

As an important LIDC directly under the Wuxi government, WUCD is mainly responsible for urban and rural construction, affordable housing construction and other functions in the region. WUCD undertakes various urban and rural construction projects in Wuxi, such as hospital, school, agent construction projects and other important city-level urban renewal and rural revitalization projects, etc. WUCD's strategic planning and development have been aligned with the local government's economic and social policies. It carries out the directions and policies of affordable housing construction of the Wuxi government to support the local economy growth.

Strong Linkage with the Wuxi Government

WUCD's linkage with the local government is strong as it is wholly owned by the Wuxi government through Wuxi SASAC. The Wuxi government has strong control and supervision over WUCD, including control of the board of directors, senior management appointments and major strategic, investing and financing plans.

Ongoing Government Support

WUCD has received supports from the local government for its business operation, which are not limited to capital injections, government subsidies, allocation of equity or assets and guidance from the government in its daily management. WUCD's capital surplus increased RMB2,312.7 million in 2021, mainly due to the proportionally recognizing Wuxi government's capital injections of RMB5,082.6 million to TNCG. At end-September 2022, the capital surplus increased RMB13.9 billion and the total equity attributable to parent company increased RMB14.4 billion as compared to the figures at end-2021, which was mainly due to the newly recorded equities of WCDI, WEPG and TNCG.

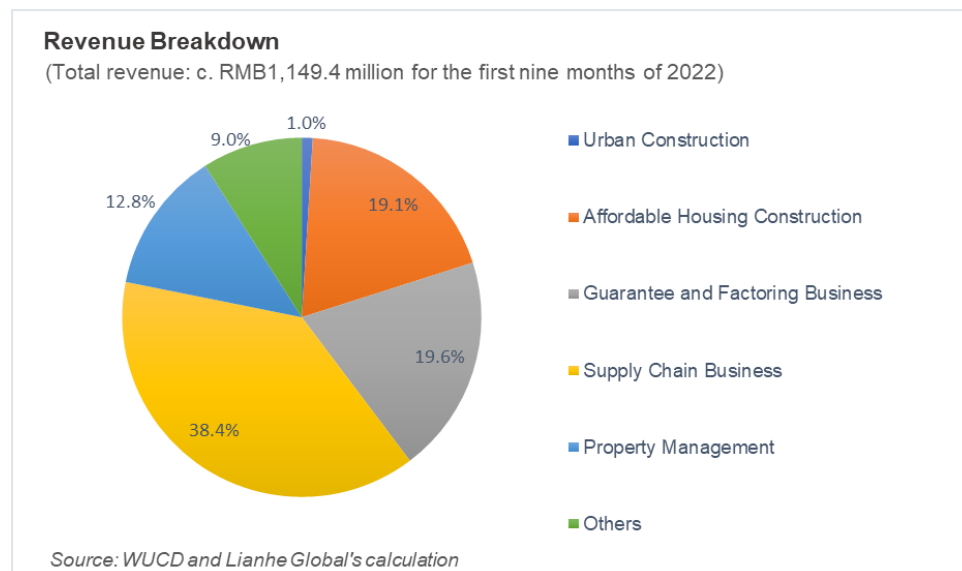
WUCD has received financial subsidies from the local government mainly for supporting business development. The company received a total of c. RMB19.48 million of government subsidies between 2019 and 2021. Besides, Wuxi Anju Investment Development Co., Ltd., a subsidiary of WUCD, received RMB179 million, RMB175 million and RMB132 million for affordable housing construction in 2019, 2020 and 2021, respectively. WUCD also benefits from preferential tax and tax exemption policies in encouraged industries. We believe WUCD is likely going to receive government support in time of operational and/or financial subsidies in the future.

Business Profile

An Important LIDC Responsible for Urban and Rural Construction and Development in Wuxi

As an important LIDC directly under the Wuxi government, WUCD is mainly responsible for urban and rural construction, affordable housing construction and other functions in the region. In addition, WUCD also engages in city operation, asset operation, financial services, etc. The total asset of WUCD was c. RMB123.3 billion at end-2021, and changed to c. RMB65.3 billion at end-September 2022, mainly because the TNCG (total asset of c. RMB95.6 billion at end-2021) was out of its consolidated scale since 2022. After the restructuring, WUCD's business and revenue structure had changed. The total revenue of the company was c. RMB2.9 billion, RMB3.6 billion, RMB4.7 billion and RMB1.1 billion in

2019, 2020, 2021 and nine months ended September 2022, respectively. The main revenue resources of WUCD changed from urban construction and real estate sales to supply chain business at end-September 2022. The gross margin of WUCD has been at the level of c. 20% - 24% during the past three years.



Urban Construction

The urban construction segment includes agent construction management and construction engineering. The agent construction management is mainly operated by WUCD and its subsidiaries. For agent construction management, WUCD signs the agent construction and management contract with the entrusting party (mainly the related administrative public institutions in Wuxi) and is responsible for the management of project, while the project funds are from the entrusting party base on the project progress. WUCD charges the agent construction management fees, which are generally 0.7%-1.5% of the total project cost. Currently, WUCD undertakes various agent construction management projects in Wuxi, such as hospital, school, etc.

The construction engineering was mainly operated by TNCG and the entrusting party was related government department in Taihu New City area. TNCG undertakes the financing, investment and construction of the project and the entrusting party will repurchase the project after its completion, with a total investment amount plus a percentage of markup (i.e., 1%-10%) and the repurchase period is 5-10 years. However, after the reorganization of TNCG, WUCD has no agent construction engineering business or land development business for the time being.

Affordable Housing Construction

According to the annually plan of affordable housing project issued by the Wuxi government, WUCD carries out the construction of affordable housing in the region. The land of related construction project is allocated by the government, while the construction funds are raised by the company itself. After the completion of the project, the relevant government department of Wuxi will determine the benchmark unit price of sales and then the company sell it to eligible low-income housing poor families in cities. In addition, some low-rental public housings are leased and managed by Wuxi Housing Security Office, and the income is directly handed over to the finance bureau. The company does not participate in the

management and rent collection of this part of houses, so the cost of this part of housing construction is not covered by income, but the relevant government department will provide financial support. At the same time, with the approval of the Wuxi government, the company is also responsible for the reconstruction of dangerous and old houses in the urban shantytowns of Liangxi District (“Liangxi”) of Wuxi and selling them to the relocated households in the region. The sales price shall be approved by the Municipal Price Bureau. In case of any loss, the Financial Department of Liangxi shall make up the loss.

Guarantee and Factoring Business

The guarantee business is mainly housing guarantee. Affected by the epidemic, the growth of Wuxi’s real estate market has slowed down in recent years, and the demand for housing guarantee has also been affected. The company signs a cooperation agreement with the Housing Provident Fund Management Center of Wuxi, which agreed that the Housing Provident Fund Management Center would purchase the loan guarantee services provided by the company at the price of RMB1,000 for each loan. In addition to the housing provident fund loan, if the applicant is involved in commercial housing loans at the same time, the company will cooperate with commercial banks in Wuxi to carry out the guarantee business of portfolio loans and charge a certain guarantee fee from the bank.

With the continuous development of the company’s factoring business, the company’s factoring revenue has grown steadily. The seller applies for factoring funds by transferring receivables to the company. After the company passes the review, it will transfer factoring funds (generally 70% or 80% of the transferred receivables) to the seller. Factoring can be divided into recourse factoring or non-recourse factoring depending on whether to exercise the right of recourse. It can also be divided into explicit factoring or implicit factoring depending on whether to send a notice to the buyer. The company also established a risk management committee to conduct supervision, control and review. Factoring receivables in the company’s accounts receivable are highly concentrated, mainly including central enterprises and state-owned enterprises.

Supply Chain Business

The supply chain business is a new business segment of WUCD after it acquired a subsidiary in February 2022. The company mainly carries out steel trade and supply chain services, providing threaded steel, spiral steel, high-speed wire, round steel, section steel and other varieties for China State Construction Engineering Corporation Ltd.’s subordinate companies, which are mainly concentrated in East and North China. The upstream and downstream customers of the company’s supply chain business are highly concentrated. It has become the largest contribution of the company’s total revenue. The revenue from this business segment was RMB441.8 million, accounted for 38.4% of its total revenue at end-September 2022.

Other Businesses

Other businesses mainly include property management, property leasing, environmental business, parking fee and others. The property management business mainly consists of management fee of residential property and business buildings in Wuxi. The properties leased by the company are mainly commercial properties, including office buildings, exhibition halls and shopping malls, which are mainly concentrated in the region. Other businesses are relatively small in scale and have limited impact for the company.

Financial Profile

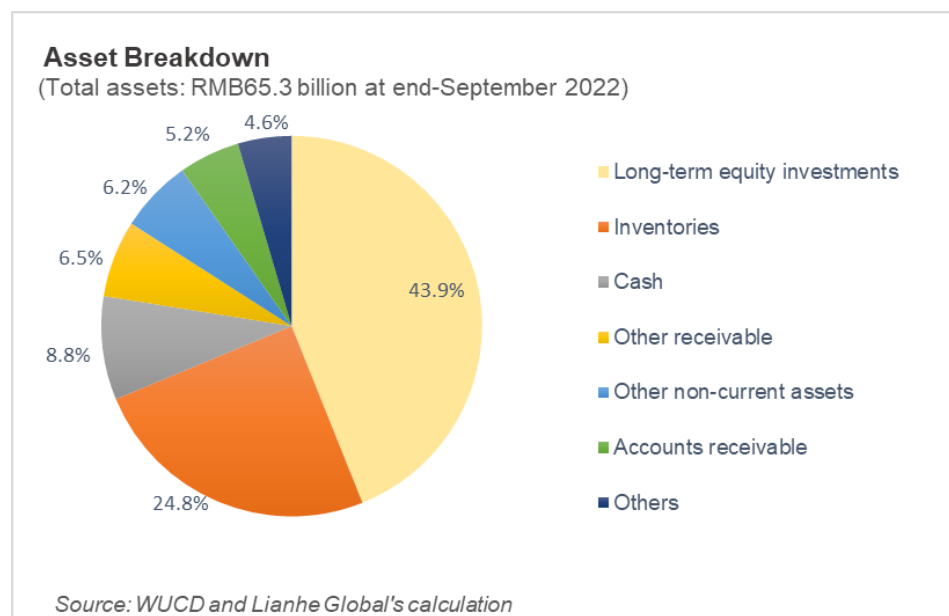
Balance Sheet Structure and Quality

Balance Sheet Structure and Quality				
(RMB million)	2019	2020	2021	Sept 2022
Total Asset	108,629	106,657	123,282	65,271
Equity	36,543	36,871	42,221	36,439
Debt	52,497	52,018	59,783	18,451
Debt / (Debt + Equity) (%)	59.0	58.5	58.6	33.6
LT Debt	38,248	38,047	47,071	12,964
LT Debt / (LT Debt + Equity) (%)	51.1	50.8	52.7	26.2

Source: WUCD's financial reports and Lianhe Global's calculations

Apart from the impact on WUCD's business, the reorganization of TNCG also led to material effects on WUCD's asset structure. As the only LIDC responsible for infrastructure construction in Wuxi Economic Development Zone, TNCG has large amount of assets in inventories, other receivables, investment properties and construction in progress, with total assets of c. RMB95.6 billion at end-2021, which accounted for 77.5% of WUCD's total assets at end-2021.

After the reorganization of TNCG, along with the equities of WCDI and WEPG transferred from the Wuxi government in January 2022, WUCD's total assets decreased by c. 47% from RMB123.3 billion at end-2021 to RMB65.3 billion at end-September 2022. The inventories, other receivables, cash, investment properties and construction in progress decreased the most among WUCD's assets. On the contrary, WUCD's long-term equity investments increased sharply from RMB0.7 billion at end-2021 to RMB28.7 billion at end-September 2022 as a result of newly recording the equity of TNCG, WCDI and WEPG as long-term equity investments, accounting for 43.9% of WUCD's total assets at end-September 2022.



Owing to the deconsolidation of TNCG, WUCD's financial leverage improved. Its leverage ratio, measured as total liabilities over total assets, improved to 44.2% at end-September 2022 from 65.8% at end-2021, while the total debt capitalization ratio declined to 33.6% at

end-September 2022 from 58.6% at end-2021. The total debts of WUCD decreased by 69.1% from RMB59.8 billion at end-2021 to RMB18.5 billion at end-September 2022.

WUCD's equity decreased by 13.7% to RMB36.4 billion at end-September 2022 from RMB42.2 billion at end-2021. The capital surplus increased RMB13.9 billion and the total equity attributable to parent company increased RMB14.4 billion as compared to the figures at end-2021, which was mainly due to the newly recorded equities of WCDI, WEPG and TNGG.

Cash Flow

Cash Flow (RMB million)	2019	2020	2021	9M2022
Cash Inflows from Operation	10,023	9,177	12,074	2,968
Cash Outflows from Operation	5,902	5,356	12,274	4,655
Net CF from Operation	4,120	3,821	-200	-1,687
Cash Inflows from Investment	18,496	6,412	3,926	944
Cash Outflows from Investment	16,035	8,399	12,668	11,142
Net CF from Investment	2,460	-1,987	-8,741	-10,198
Cash Inflows from Financing	18,692	21,681	40,231	6,830
Cash Outflows from Financing	25,050	25,982	28,685	3,975
Net CF from Financing	-6,358	-4,301	11,546	2,855
Net Increase in Cash and cash equivalent	223	-2,467	2,604	-9,031

Source: WUCD's financial reports

Debt Servicing Capability

The liquidity of WUCD was relatively adequate. At end-September 2022, WUCD had a cash balance of c. RMB5.7 billion (restricted cash was approximately RMB0.1 billion) and a total credit line of RMB36.3 billion, of which approximately RMB26.3 billion was available, compared with its debt to be due within one year of c. RMB5.5 billion. WUCD has access to multiple financing channels including bank borrowings, corporate bonds and other financing channels such as trust loan and finance lease.



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