

Shanghai Zhuanghang Economic Development Co., Ltd.

Initial Issuer Report

Summary

Issuer Rating	BBB-
Outlook	Stable
Location	China
Industry	Local Investment and Development Companies
Date	31 March 2023

Lianhe Ratings Global Limited (“Lianhe Global”) has assigned ‘BBB-’ global scale Long-term Issuer Credit Rating with Stable Outlook to Shanghai Zhuanghang Economic Development Co., Ltd. (“SZED” or “the company”)

Summary

The Issuer Credit Rating reflects a high possibility that the People’s Government of Fengxian District of Shanghai City (“Fengxian government”) would provide moderately strong support to SZED if needed, in light of its indirect full ownership of SZED, SZED’s strategic importance as an important local investment and development company (“LIDC”) responsible for infrastructure construction in Zhuanghang Town (“Zhuanghang”) of Fengxian District (“Fengxian”), and the linkage between the Fengxian government and SZED, including appointment and supervision of the senior management, strategic alignment, major investment and financing plan decisions and ongoing government support, etc. In addition, the Fengxian government may face negative impact on its reputation and financing activities if SZED encounters any operational and financial difficulties.

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

Rating Rationale

Government’s Ownership and Supervision: SZED was established in August 2009. The Zhuanghang government, through several village committees and other state-owned entities, holds 100% ownership of SZED. Zhuanghang is one of the eight towns under Fengxian. The Fengxian government has strong supervision over the company, including appointment and supervision of the senior management, strategy alignment and major investment and financing plan decisions, etc. In addition, the Fengxian government has formulated a performance appraisal policy for the company, and regularly appoints auditors to review the company’s operating performance and financial position.

Strategic Importance and Strategic Alignment: SZED is an important state-owned entity for infrastructure construction in Zhuanghang that mainly undertakes the construction of municipal projects and landscaping projects. SZED has a leading position in infrastructure construction in the region and it plays an important role for urban construction and development. The development strategy of the company is aligned with the development plan of the local government, aiming to follow by the “14th Five-Year Plan” of the local government and to promote local urban and rural construction and development.

Ongoing Government Support: As an important state-owned entity for infrastructure construction in Zhuanghang, the company continuously received government support, including policy support, project and capital support, etc. In 2012, the registered and paid-in capital of the company both increased from the initial of RMB1 million to RMB25 million, mainly increased by capital injection from shareholder. In addition, the company also continuously received subsidies from the local government. Given the company’s function and importance, we believe that the company is likely going to receive timely government support in the form of operational and/or financial subsidies in the future.

Key Figures of Fengxian and SZED

(RMB billion)	2021	2022
Fengxian District		
GDP	133.0	137.1
GDP growth rate (%)	9.3	0.4
Budgetary revenue	22.1	22.2
Government fund	13.9	15.8
Transfer payment	15.0	14.7
Budgetary expenditure	33.3	33.7
SZED		
Assets	17.9	20.7
Equity	13.0	14.1
Revenue	0.4	0.5

Source: Public information, SZED and Lianhe Global’s calculations

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Applicable Criteria

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

SZED's Financial and Liquidity Position: SZED's total asset grew steadily and the asset structure was relatively stable in the past few years. At end-2022, SZED's assets were mainly composed of land, construction projects, receivables and investment properties. Although the company's asset structure was dominated by current assets, the use of some assets was restricted and accounts receivable occupied funds, thus, the company's overall asset liquidity was moderately weak. The financial leverage ratio (total liabilities/total assets) of SZED was 31.9% at end-2022. The company mainly relies on external financing to support its capital expenditure. At end-2022, the company's adjusted debt was c. RMB5.1 billion, of which short-term debt and long-term debt accounted for 20.1% and 79.9% of its total debt, respectively, and the company's short-term repayment pressure was relatively small.

Economy and Fiscal Condition of Fengxian: Fengxian is a district of Shanghai and it is located in the south of Shanghai. Fengxian is the southern gate and important transportation hub of Shanghai connecting with Shanghai and Zhejiang coastal areas. Its GDP reached c. RMB137.1 billion in 2022, representing a year-on-year growth rate of 0.4%. The aggregate fiscal revenue of the Fengxian government was mainly derived from the budgetary revenue and government fund income. In 2022, affected by the value-added tax (VAT) credit refund policy, the budgetary revenue of Fengxian was c. RMB22.2 billion, and the percentage of tax revenue decreased to 86.6% from 91.7% in 2020. The financial self-sufficiency rate of Fengxian was insufficient and it recorded budget deficit of 51.4% in 2022. Nevertheless, Fengxian continuously received subsidies from higher government. The government fund income of Fengxian increased by 13.6% to RMB15.8 billion in 2022. At end-2022, the Fengxian government's outstanding debt was c. RMB49.5 billion, including RMB31.2 billion of general obligations and RMB18.3 billion of special debt.

Rating Sensitivities

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

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

Operating Environment

Economic Condition of Fengxian

Fengxian is a district of Shanghai and it is located in the south of Shanghai, bordering Pudong New Area in the east. Fengxian is the southern gate and important transportation hub of Shanghai connecting with Shanghai and Zhejiang coastal areas. Fengxian has jurisdiction over 8 towns, 3 streets and Shanghai Fengxian Bay tourism area with a total land area of 733.38 square kilometers. The residential population of Fengxian was c. 1.1 million with an urbanization rate of c. 60% at end-2022.

Fengxian maintained economic growth but slightly slowed down in 2022. Its GDP reached c. RMB137.1 billion in 2022, representing a year-on-year growth rate of 0.4%. Fengxian's GDP amount was ranked 11th in Shanghai in 2022 (out of a total 16 districts). The economic structure of Fengxian was stable, which was mainly fueled by the secondary and tertiary industries, accounting for 64.3% and 35.0% of its GDP in 2022. GDP per capita of Fengxian was c. RMB119,500 in 2022, which was higher than the GDP per capita of China (c. RMB85,700) but lower than that of Shanghai's (c. RMB179,400). In addition, affected by the decline in real estate investment, the decline in fixed asset investment of Fengxian in 2022 was more obvious.

Fengxian's GDP and Fixed Asset Investment

(RMB billion)	2020	2021	2022
GDP	119.0	133.0	137.1
-Primary industry (%)	0.9	0.7	0.7
-Secondary industry (%)	63.0	63.9	64.3
-Tertiary industry (%)	36.1	35.4	35.0
GDP growth rate (%)	2.0	9.3	0.4
Fixed asset investment	52.7	58.1	54.2
Fixed asset investment growth rate (%)	13.1	10.2	-6.8
Population (million)	1.1	1.1	1.1

Source: Public information and Lianhe Global's calculations

Fiscal Condition of Fengxian

The aggregate fiscal revenue of the Fengxian government was mainly derived from the budgetary revenue and government fund income. In 2022, affected by the value-added tax (VAT) credit refund policy, the budgetary revenue of Fengxian was c. RMB22.2 billion, and the percentage of tax revenue decreased to 86.6% from 91.7% in 2020. The financial self-sufficiency rate of Fengxian was insufficient and it recorded budget deficit of 51.4% in 2022. Nevertheless, Fengxian continuously received subsidies from higher government. The government fund income of Fengxian increased by 13.6% to RMB15.8 billion in 2022, mainly due to the increase in land transfer income.

The outstanding debt of the Fengxian government continued to grow. At end-2022, the Fengxian government's outstanding debt was c. RMB49.5 billion, including RMB31.2 billion of general obligations and RMB18.3 billion of special debt. Given the Fengxian government borrowed heavily in special debts to support its public projects, its fiscal debt ratio, as measured by total government debt outstanding/aggregate revenue, increased to c. 93.5% at end-2022.

Fengxian's Fiscal Condition (RMB billion)	2020	2021	2022
Budgetary revenue	16.2	22.1	22.2
Budgetary revenue growth rate (%)	4.3	36.6	² 6.1
Tax revenue	14.8	19.4	19.3
Tax revenue (% of budgetary revenue)	91.7	88.0	86.6
Government fund income	13.4	13.9	15.8
Transfer payment	12.0	15.0	14.7
Aggregate revenue	41.8	51.1	52.9
Budgetary expenditure	25.9	33.3	33.7
Budget deficit ¹ (%)	-60.4	-50.6	-51.4

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

² Excluding the influence of value-added tax credit refund.

Source: Public information and Lianhe Global's calculations

Ownership Structure

Government's Ownership

SZED was established in August 2009. The Zhuanghang government, through several village committees and other state-owned entities, holds 100% ownership of SZED. Zhuanghang is one of the eight towns under Fengxian. At end-2022, the registered and paid-in capital of SZED were both RMB25 million.

Strategic Importance and Government Linkage

Strategic Importance of SZED to Zhuanghang Town of Fengxian District

SZED is an important state-owned entity for infrastructure construction in Zhuanghang mainly undertakes the construction of municipal projects and landscaping projects. SZED has a leading position in infrastructure construction in the region and it plays an important role for urban construction and development. The development strategy of the company is aligned with the development plan of the local government, aiming to follow by the "14th Five-Year Plan" of the local government and to promote local urban and rural construction and development.

Linkage with the Local Government

The Fengxian government has strong supervision over the company, including appointment and supervision of the senior management, strategy alignment and major investment and financing plan decisions, etc. In addition, the Fengxian government has formulated a performance appraisal policy for the company, and regularly appoints auditors to review the company's operating performance and financial position.

Ongoing Government Support

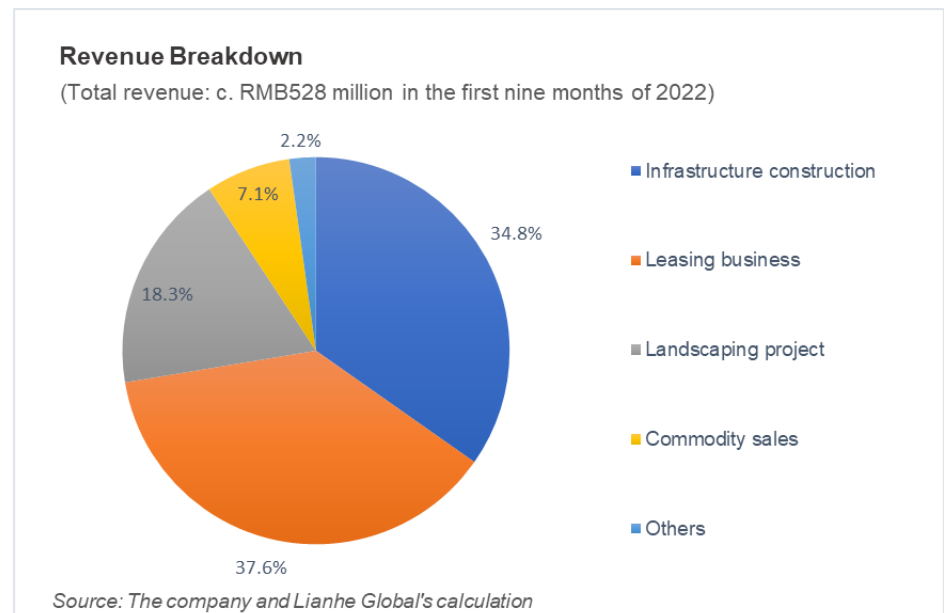
As an important state-owned entity for infrastructure construction in Zhuanghang, the company continuously received government support, including policy support, project and capital support, etc. In 2012, the registered and paid-in capital of the company both increased from the initial of RMB1 million to RMB25 million, mainly increased by capital injection from shareholder. In addition, the company also continuously received subsidies from the local government. Given the company's function and importance, we believe that

the company is likely going to receive timely government support in the form of operational and/or financial subsidies in the future.

Business Profile

The Important LIDC Responsible for Infrastructure Construction in Zhuanghang of Fengxian of Shanghai

The company is an important state-owned entity for infrastructure construction in Zhuanghang that mainly undertakes the construction of municipal projects and landscaping projects in the region. The main businesses of the company include agent construction project, landscaping project, leasing, trading business and other business. The major revenue sources of the company are infrastructure construction income and leasing income.



Infrastructure Construction and Landscaping Construction

The company is an important state-owned entity for infrastructure construction in Zhuanghang and it mainly undertakes the infrastructure construction and landscaping construction projects in Zhuanghang. The company is entrusted by the Zhuanghang government and the Finance Office, responsible for the construction of roads, greening, renovation project and other agent construction projects in Zhuanghang area. According to the agent construction agreement, the company shall be responsible for the construction cost of the project. After the completion of the project, the Zhuanghang government or Finance Office shall settle the construction fee with the company, and the construction fee shall be settled according to the project settlement cost plus a certain percentage (generally 20%) as project income. At present, the company has several projects under construction, and there are capital expenditure pressures in the future.

Leasing Business

The company's leasing income mainly comes from renting out its own property such as business building and other office plants, and collecting rent. The volatility of rental income

has decreased as the pandemic has eased. In the future, as more self-owned properties will be rented out, the scale of leasing income of the company will be increased. In addition, the gross profit rate of this business is expected to increase gradually, which will improve the comprehensive gross profit of the company.

Other Business

The company's other businesses mainly include commodity sales, consulting services, etc. The scale of other business income is relatively small, but the gross profit rate is high, which plays a certain role in improving the company's profitability.

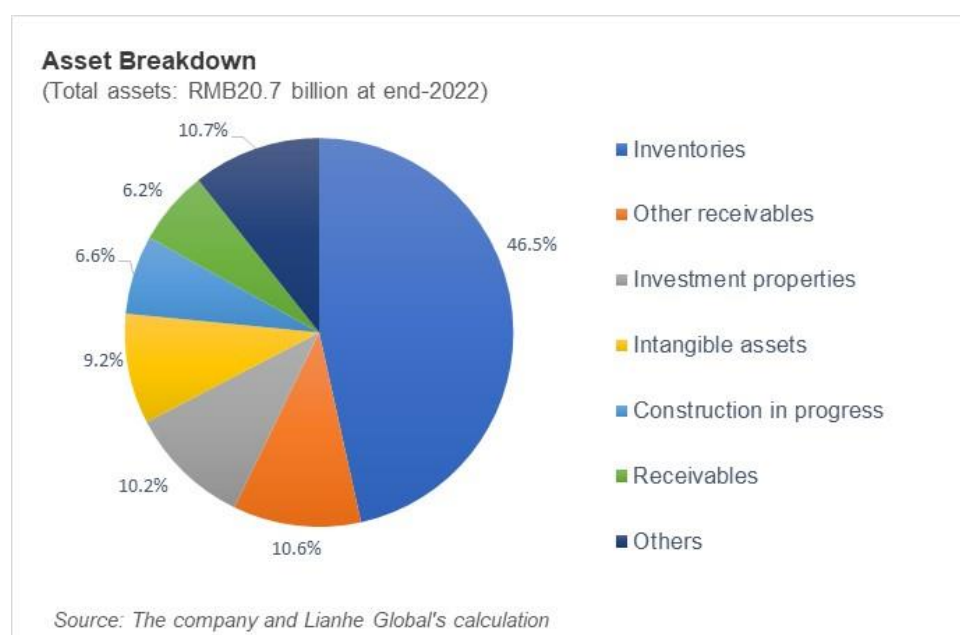
Financial Profile

Balance Sheet Structure and Quality

Balance Sheet Structure and Quality			
(RMB million)	2020	2021	2022
Total Asset	14,903	17,875	20,719
Equity	10,569	12,966	14,117
Debt	3,424	3,586	5,060
Debt / (Debt + Equity) (%)	24.5	21.7	26.4
LT Debt	2,694	2,601	4,044
LT Debt / (LT Debt + Equity) (%)	20.3	16.7	22.3

Source: The company's financial reports and Lianhe Global's calculations

The financial leverage ratio (total liabilities/total assets) of SZED was relatively low at c. 30% in 2020-2022, which was 31.9% at end-2022. The company's liabilities were mainly consisted of long-term receivables and other receivables, of which the long-term receivables were mainly financial leasing amount. As the company adopts agent construction mode for project construction, the company mainly relies on external financing (mainly takes long-term loans and project loans) to support its capital expenditure. At end-2022, the company's adjusted debt was c. RMB5.1 billion, of which short-term debt and long-term debt accounted for 20.1% and 79.9% of its total debt, respectively, and the company's short-term repayment pressure was relatively small.



SZED's total asset grew steadily and the asset structure was relatively stable in the past few years. At end-2022, SZED's assets were mainly composed of land, construction projects, receivables and investment properties. The scale of inventory was large that mainly included land to be developed and construction project. The receivables of the company were mainly current accounts of Zhuanghang government and other government related entities, with a relatively low collection risk. The investment properties of the company were its own properties that used for rent. Although the company's asset structure was dominated by current assets, the use of some assets was restricted and accounts receivable occupied funds, thus, the company's overall asset liquidity was moderately weak.

Cash Flow

Cash Flow (RMB million)	2020	2021	2022
Cash Inflows from Operation	1,162	1,079	1,606
Cash Outflows from Operation	964	1,009	1,030
Net CF from Operation	198	70	577
Cash Inflows from Investment	24	-	-
Cash Outflows from Investment	244	511	396
Net CF from Investment	-219	-511	-396
Cash Inflows from Financing	458	761	383
Cash Outflows from Financing	409	300	551
Net CF from Financing	49	462	-168
Net Increase in Cash and cash equivalent	27	21	12

Source: The company's financial reports

Debt Servicing Capability

The liquidity risk of SZED was relatively small. The company's total adjusted debt was c. RMB5.1 billion at end-2022, of which short-term and long-term debt accounted for 20.1% and 79.9% of its total adjusted debt, respectively. At end-2022, SZED had a cash balance of c. RMB870.6 million and unused credit facilities of c. RMB1.2 billion, compared with its debt due within one year of c. RMB1.0 billion. SZED mainly relied on external financing to support its capital expenditure with limited financing channels, which was mainly bank loans.

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