

# Xiao County Construction Investment Group Co., Ltd.

## Initial Issuer Report

### Summary

Issuer Rating	BBB-
Outlook	Stable
Location	China
Industry	Local Investment and Development Companies
Date	18 May 2023

### Key Figures of Xiao County and XCCIG

(RMB billion)	2021	2022
Xiao County		
GDP	41.7	43.2
GDP growth rate (%)	8.5	5.1
Budgetary revenue	2.4	2.1
Government fund	2.8	2.9
Transfer payment	4.2	4.5
Budgetary expenditure	7.7	8.0
XCCIG		
Assets	2.9	10.6
Equity	1.2	7.2
Revenue	0.2	0.2

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

Lianhe Ratings Global Limited ("Lianhe Global") has assigned 'BBB-' global scale Long-term Issuer Credit Rating with Stable Outlook to Xiao County Construction Investment Group Co., Ltd. ("XCCIG" or "the company")

### Summary

The Issuer Credit Rating reflects a high possibility that the People's Government of Xiao County, Suzhou City ("Xiao County government") would provide very strong support to XCCIG if needed, in light of its direct full ownership of XCCIG, XCCIG's strategic importance as the key local investment and development company ("LIDC") that is responsible for comprehensive urban operation, project construction, area development and state-owned asset management in Xiao County, Suzhou City ("Xiao County"), and the linkage between the Xiao County government and XCCIG, including appointment and supervision of the senior management, strategic alignment, major investment and financing plan decisions and ongoing operational and financial support. In addition, the Xiao County government may face significant negative impact on its reputation and financing activities if XCCIG encounters any operational and financial difficulties.

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

### Rating Rationale

**Xiao County Government's Ownership and Supervision:** The Xiao County government directly holds 100% ownership of XCCIG through the Finance Bureau of Xiao County, Suzhou City ("Xiao County FB"), and is the actual controller of the company. The Xiao County government has the final decision-making authority and supervises the company, including management appointment, decision on its strategic development and investment plan and supervision of its major funding decisions. In addition, the Xiao County government has assessment mechanism over the company and it appoints auditor to supervise the operating performance and financial position on a periodic basis.

**Strategic Importance to Xiao County and Strategic Alignment:** XCCIG, as the main implementation body for comprehensive urban operation, state-owned asset management and project construction in Xiao County, is primarily responsible for the construction of key urban projects, sewage treatment, water supply, urban maintenance and management in Xiao County, as well as the area development within the area, with strong franchised advantages. XCCIG serves as the primary platform for urban construction financing and manages urban construction funds. It plays an important role in promoting the economic and social development and of Xiao County. Its business operation and development have been aligned with the government's development plans.

**Ongoing Government Support:** XCCIG received operational and financial support from the government. XCCIG received a total subsidy amount of c. RMB76.8 million from 2020 to 2022, mainly including operating subsidies. Meanwhile, the Xiao County government continued to inject cash, equity, investment properties and other assets into XCCIG to expand its asset size. Besides, the government will provide policy supports to XCCIG to ensure its business operation. Given the franchise advantages in project construction, area development and urban operation, XCCIG has advantage to obtain major projects. We

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### Applicable Criteria

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

believe XCCIG is likely going to receive government support in the form of operational and/or financial subsidies to support its daily business operation.

**XCCIG's Financial Matrix and Liquidity Position:** XCCIG's total assets showed a continuous growth trend in the past years and reached RMB10.6 billion at end-2022 mainly due to the receiving of equities and investment properties from the Xiao County government. The current assets of XCCIG accounted for c. 56.7% of the total assets at end-2022, but the overall assets were less liquid, due to high development cost and large-scale investment properties and receivables. XCCIG's financial leverage (total liabilities to assets) remained stable at c. 58% from end-2020 to end-2021, but decreased to 31.9% at end-2022. XCCIG's adjusted total debt increased to c. RMB3.2 billion at end-2022. The liquidity of XCCIG was sufficient. At end-2022, XCCIG had unrestricted cash balance and unused credit facilities of c. RMB42.3 million and RMB1.8 billion, respectively, compared with its debt due within one year of c. RMB1.0 billion at the same time. Besides, XCCIG has access to various financing channels, including bank loans and non-traditional financing, to support its debt repayment and business operations.

**Economy and Fiscal Condition of Xiao County:** Xiao County is located in the northwest of Suzhou City, Anhui Province ("Suzhou"). It recorded an economic growth in 2022, achieving a GDP of c. RMB43.2 billion, with a year-on-year growth of 5.1%. Its total GDP ranks second among all districts and counties in Suzhou. The aggregate fiscal revenue of the Xiao County government was mainly derived from the budgetary revenue and government fund income. In 2022, the budgetary revenue of the Xiao County government decreased to c. RMB2.1 billion, due to the large-scale value-added tax credit refunds to support the economy. At the same time, the government fund income maintained steady growth, reaching c. RMB2.9 billion in 2022. The financial self-sufficiency rate of Xiao County was insufficient and it recorded a budget deficit of -289.9% in 2022. Its fiscal debt ratio, as measured by total government debt outstanding/aggregate revenue, increased to 118.8% at end-2022 from 78.6% at end-2020.

## Rating Sensitivities

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

We would consider upgrading XCCIG's rating if (1) there is an upgrade in our internal credit assessment on the Xiao County government.

## Operating Environment

### Economic Condition of Xiao County

Xiao County is a county of Suzhou and is located in the northwest of Suzhou. Xiao County is a time-honored city with many historic and cultural sites. Besides, the county is also famous for painting, calligraphy and folk arts. Xiao County has jurisdiction with 23 towns, 3 streets and 1 economic development zone, with a total land area of c. 1,853.6 square kilometers. At end-2022, Xiao County has a population of c. 1.0 million.

Xiao County maintained steady economic growth in recent few years. Its GDP reached c. RMB43.2 billion in 2022, representing a year-on-year growth rate of 5.1%. Xiao County's GDP amount was ranked 2<sup>nd</sup> out of all counties of Suzhou in 2022. The economic growth of Xiao County was mainly boosted by the secondary and tertiary industries, which accounted

for 41.4% and 41.1% of GDP in 2022, respectively. The fixed asset investment achieved moderate growth in the past three years and reached c. RMB59.5 billion in 2022.

<b>Xiao County's GDP and Fixed Asset Investment</b>			
<b>(RMB billion)</b>	<b>2020</b>	<b>2021</b>	<b>2022</b>
GDP	39.3	41.7	43.2
-Primary industry (%)	17.8	17.8	17.5
-Secondary industry (%)	42.0	42.1	41.4
-Tertiary industry (%)	40.2	40.1	41.1
GDP growth rate (%)	4.1	8.5	5.1
Fixed asset investment	47.9	53.9	59.5
Fixed asset investment growth rate (%)	6.5	12.6	10.4
Population (million)	1.1	1.0	1.0

Source: Public information and Lianhe Global's calculations

## Fiscal Condition of Xiao County

The aggregate fiscal revenue of the Xiao County government was mainly derived from the government fund income and transfer payment. Government fund income maintained steady growth in the past three years, reaching c. RMB2.9 billion in 2022, which was mainly derived from land sales. The transfer payment increased from c. RMB4.2 billion in 2021 to c. RMB4.5 billion in 2022, accounting for nearly half of the aggregate fiscal revenue. The budgetary revenue of the Xiao County government fluctuated in the past three years, and reached c. RMB2.9 billion in 2022, representing a year-on-year decrease of 11.9%. The tax revenue accounted for 53.7%-58.2% of the budgetary revenue in 2020-2022. The financial self-sufficiency rate of Xiao County was insufficient and it recorded a budget deficit of -289.9% in 2022.

The outstanding debt of the Xiao County government increased year by year and reached c. RMB11.2 billion at end-2022, which included c. RMB4.1 billion of general obligations and c. RMB7.2 billion of special debt. Given the Xiao County 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 118.8% at end-2022 from 78.6% at end-2020.

<b>Xiao County's Fiscal Condition</b>			
<b>(RMB billion)</b>	<b>2020</b>	<b>2021</b>	<b>2022</b>
Budgetary revenue	2.2	2.4	2.1
Budgetary revenue growth rate (%)	0.6	5.0	-11.9*
Tax revenue	1.3	1.3	1.1
Tax revenue (% of budgetary revenue)	58.2	55.2	53.7
Government fund income	2.7	2.8	2.9
Transfer payment	5.3	4.2	4.5
<b>Aggregate revenue</b>	<b>10.2</b>	<b>9.3</b>	<b>9.4</b>
Budgetary expenditure	8.3	7.7	8.0
Budget deficit <sup>1</sup> (%)	-272.6	-228.8	-289.9

<sup>1</sup> Budget deficit = (1-budgetary expenditure / budgetary revenue) \* 100%

Note\*: Excluding the influence of value-added tax credit refund

Source: Public information and Lianhe Global's calculations

## Ownership Structure

### Government's Ownership

XCCIG was established in July 2016 with an initial registered capital of RMB2 billion. At end-2022, XCCIG's registered and paid-in capital was both RMB2 billion. The Xiao County government holds 100% shares of XCCIG through the Xiao County FB.

## Strategic Importance and Government Linkage

### Strategic Importance of XCCIG to Xiao County

In 2022, following the guidance of the Xiao County government, Xiao County completed the reorganization of state-owned enterprises, where the 19% equities of two LIDCs, namely Xiao County Construction Investment Co. Ltd. ("XCCI") and Xiao County Industrial Investment Co. Ltd. ("XCII"), were transferred to XCCIG. XCCIG, as the key LIDC in Xiao County, is primarily responsible for comprehensive urban operation, state-owned asset management and project construction in Xiao County. It is in charge of the construction of key urban projects, sewage treatment, water supply, urban maintenance and management, as well as the construction and development of Xiao County's New District, with strong franchised advantages. Additionally, XCCIG serves as the primary platform for urban construction financing and manages urban construction funds. XCCIG plays an important role in promoting the economic and social development and of Xiao County. Its business operation and development have been aligned with the government's development plans.

### Linkage with the Local Government

XCCIG's linkage with the local government is strong as the Xiao County government directly holds 100% ownership of XCCIG through the Xiao County FB. The Xiao County government has the final decision-making authority and supervises the company, including management appointment, decision on its strategic development and investment plan and supervision of its major funding decisions. In addition, the Xiao County government has assessment mechanism over the company and it appoints auditor to supervise the operating performance and financial position on a periodic basis.

### Government Support

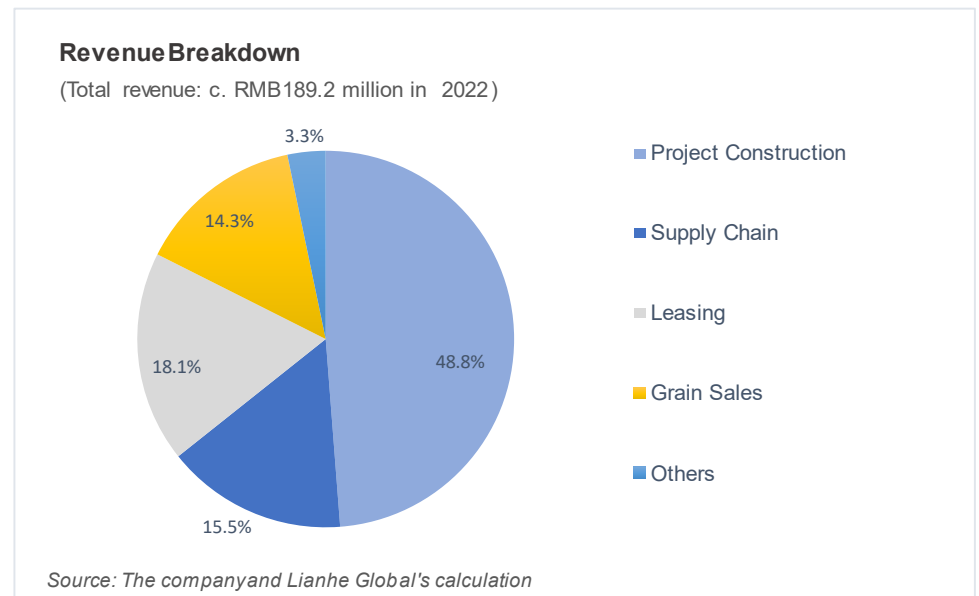
XCCIG continued to receive financial subsidies, mainly including operating subsidies from the local government to maintain its business operation. XCCIG received subsidies of c. RMB22.6 million, RMB27.0 million and RMB27.2 million in 2020, 2021 and 2022, respectively. Meanwhile, the Xiao County government continued to inject cash, equity, investment properties and other assets into XCCIG to expand its asset size, which reached RMB364.2 million and RMB5.9 billion in 2021 and 2022, respectively. In 2022, Xiao County government transferred 19% equities of the other two LIDCs in the region to the company without compensation. Besides, the government will provide policy supports to XCCIG to ensure its business operation. Given the franchise advantages in project construction, area development and urban operation, XCCIG has advantage to obtain major projects. We believe XCCIG is likely going to receive government support in the form of operational and/or financial subsidies to support its daily business operation.

## Business Profile

### The Essential Entity Responsible for Project Construction and Land Development in Xiao County

As a key LIDC in Xiao County, XCCIG mainly takes charge of infrastructure related project construction and state-owned asset management, comprehensive urban operation and some other businesses within the region. As a wholly state-owned enterprise, the company is positioned as the carrier of city operations, the platform of city construction financing and the primary resource of construction funding. Since its establishment, the company has engaged in the construction of many key infrastructure projects in Xiao County, and played an important role in promoting economic and social development within the region.

The main sources of operating revenue for XCCIG are project construction, supply chain business, leasing and other businesses. The company's total revenue reached RMB37.5 million, RMB131.6 million, RMB152.9 million and RMB189.2 million in 2019, 2020, 2021, and 2022, respectively.



### Project Construction

As an important regional LIDC, XCCIG enjoys a certain monopoly position in project construction, which was mainly handled by the company and its subsidiary, namely Xiao County Construction Investment Project Management Co. Ltd. The Xiao County government signs entrustment agreements with the company and its subsidiary, and authorizes the company to conduct the full process management of all government investment, equity participation and holding projects within the region. The company is mainly responsible for the surveying and mapping, construction and inspection of the entrusted projects. XCCIG's project construction income reached RMB26.4 million, RMB76.6 million, RMB94.3 million and RMB92.3 million in 2019, 2020, 2021 and 2022, respectively, with a stable gross margin of 17%-18%. Benefiting from the abundant experience in project construction and its strategic importance in Xiao County, XCCIG's market position will be further cemented and strengthened in the future.

### Comprehensive Urban Operation

XCCIG is instrumental in the urban operation of Xiao County. It is actively involved in the construction and operation of various urban public services, including supply chain services, driving license services, intelligent parking, sewage treatment, and water supply. XCCIG is dedicated in gradually establishing a comprehensive urban operation platform with a well-planned layout, expanding the industrial chain, and enhancing its scale and professional capabilities. Besides, XCCIG holds the exclusive responsibility as the sole LIDC for sewage treatment and water supply in Xiao County. It leverages its robust franchise advantages to effectively manage and oversee sewage treatment and water supply operations throughout the entire county.

### Other Businesses

Except for construction and urban operation businesses, XCCIG also operates other businesses such as commodity sales and leasing. As an important source of revenue for XCCIG, the commodity sales segment makes the company's business more diversified and plays a complementary role to its main business. XCCIG is mainly engaged in the grain sales. The revenue generated from the trading segment reached c. RMB10.5 million, RMB17.9 million, RMB17.6 million and RMB27.1 million in 2019, 2020, 2021 and 2022, respectively.

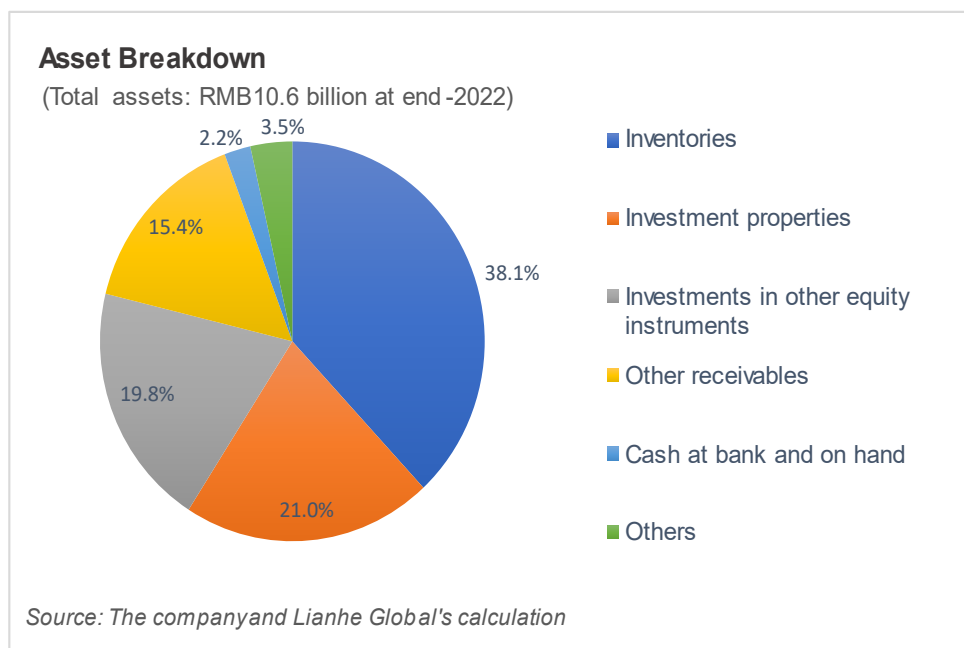
## Financial Profile

### Balance Sheet Structure and Quality

<b>Balance Sheet Structure and Quality</b>			
<b>(RMB million)</b>	<b>2020</b>	<b>2021</b>	<b>2022</b>
Total Asset	1,864	2,853	10,590
Equity	778	1,204	7,208
Debt	1,024	1,581	3,247
Debt / (Debt + Equity) (%)	56.8	56.8	42.1
LT Debt	402	421	2,232
LT Debt / (LT Debt + Equity) (%)	34.1	25.9	23.6

*Source: Company information and Lianhe Global's calculations*

XCCIG's total assets showed a continuous growth in the past few years, with a growth rate of 53.1% and 271.2% at end-2021 and end-2022, respectively, and reached RMB10.6 billion at end-2022. The increase of XCCIG's total assets in 2022 was due to higher investment properties and investments in other equity instruments. This increase was a result of receiving equities of the other two LIDCs' equities and investment properties transferred by the Xiao County government. At end-2022, XCCIG's assets mainly consisted of inventories, investment properties, investments in other equity instruments, other receivables and cash at bank and on hand. The inventories included development costs associated with XCCIG's urban-rural construction land transition projects and engineering construction related to its main operation business. Investment properties included buildings and land use rights. Other receivables were mainly transactions with other LIDCs within the region, with an aging period of mostly more than 1-year, controllable counterparty risk and low bad debt provision. Investments in other equity instruments consisted of equities of XCCI and XCII. XCCIG's current assets accounted for a relatively large proportion of total assets, reaching 56.7% at end-2022. Its assets were illiquid, primarily due to the large proportion of costs associated with construction projects, investment properties and receivables.



XCCIG's financial leverage (total liabilities to assets) remained stable at c. 58% from end-2020 to end-2021, but decreased to 31.9% at end-2022, mainly due to significant asset and equity injections provided by the local government. Its adjusted total debt increased from c. RMB1.0 billion at end-2020 to c. RMB3.2 billion at end-2022, mainly due to the increase in long-term borrowings. The short-term debt and long-term debt accounted for c. 31.2% and 68.8% of the total debt at end-2022, respectively. There was no significant change in the ownership equity structure of XCCIG at end-2022, compared with that at end-2020. The capital surplus increased to c. RMB6.5 billion at end-2022 from c. RMB237.6 million at end-2020. XCCIG mainly relies on external financing to support its capital expenditures and debt repayments, which we expect to increase in the future given its projects under construction and to be constructed in the future.

### Debt Servicing Capability

The liquidity of XCCIG was sufficient. At end-2022, XCCIG had unrestricted cash balance and unused credit facilities of c. RMB42.3 million and RMB1.8 billion, respectively, compared with its debt due within one year of c. RMB1.0 billion at the same time. Besides, XCCIG has access to various financing channels, including bank loans and non-traditional financing, to support its debt repayment and business operations.

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