

Xinyi High-tech Construction Development Group Co., Ltd. Initial Issuer Report

Lianhe Ratings Global Limited (“Lianhe Global”) has assigned ‘BBB-’ global scale Long-term Issuer Credit Rating with Stable Outlook to Xinyi High-tech Construction Development Group Co., Ltd. (“XHCD” or “the company”)

Summary

The Issuer Credit Rating reflects a high possibility that the Xinyi People’s Government (“the Xinyi government”) would provide strong support to XHCD if needed, in light of its full ownership of XHCD, XHCD’s strategic importance as an important local investment and development company (“LIDC”) responsible for land development, infrastructure construction and urban village renovation, as well as industrial parks development and operation in Xiyi High-tech Industrial Development Zone (“High-tech Zone”), and the linkage between the Xinyi government and XHCD, including the appointment of the senior management, strategic alignment, supervision of major financing plan and investment decisions and ongoing operational and financial support. In addition, the Xinyi government may face significant negative impact on its reputation and financing activities if XHCD encounters any operational and financial difficulties.

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

Rating Rationale

Government’s Ownership and Supervision: The Xinyi government holds 100% shares of XHCD directly. The local government also has strong control over the company, including the appointment of senior management and supervision of development strategy, major financing plan and investment decisions. In addition, the local government has formulated a performance assessment policy for the company, and regularly appoints auditors to review the company’s operating performance and financial position.

Strategic Importance and Strategic Alignment: XHCD’s strategic development plan has been aligned with the local government’s economic and social policies. It is the key LIDC responsible for project construction, including land development, infrastructure construction and urban village renovation, in High-tech Zone, a provincial-level development zone focusing on the electronic information, machinery manufacturing, biopharmaceuticals, light textile, and logistics processing industry. The company also develops and operates industrial parks in High-tech Zone to promote Xinyi’s industrial and economic development.

Ongoing Government Support: XHCD received ongoing operational subsidies from the Xinyi government in relation to providing public services between 2020 and 2022. In addition, XHCD received multiple capital injections, including cash, completed projects, lands, etc., over the same period. Considering its strategic importance in Xinyi, we expect the company to continue receiving government support in the future.

Summary

Issuer Rating	BBB-
Outlook	Stable
Location	China
Industry	Local Investment and Development Companies
Date	23 May 2023

Key Figures of Xinyi and XHCD (RMB billion)

	2021	2022
Xinyi		
GDP	78.1	82.6
GDP growth rate (%)	10.1	4.7
Budgetary revenue	4.4	4.6
Government fund	5.1	6.3
Transfer payment	4.7	5.1
Budgetary expenditure	10.3	10.4
XHCD	2021	2022
Asset	34.7	40.1
Equity	26.7	30.8
Revenue	0.91	0.96

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

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Applicable Criteria

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



Economy and Fiscal Condition of Xinyi: Xinyi's GDP growth rate fluctuated in the past three years, owing to Covid's disruption, which was 3.1%, 10.1% and 4.7% in 2020, 2021 and 2022, respectively. It realized a GDP of RMB82.6 billion in 2022 and was ranked 4th among ten districts and counties under the administration of Xuzhou. In recent years, Xinyi's economic development focused on manufacturing, biological, pharmaceutical and chemical industries. Its economic growth was mainly fueled by the secondary and tertiary sectors, which accounted for 39.0% and 49.3% of GDP in 2022, respectively.

The Xinyi government's budgetary revenue increased to RMB4.6 billion in 2022 from RMB3.8 billion in 2020. However, the tax revenue's contribution decreased to 70.7% from 85.9% over the same period. Xinyi's budgetary deficit was improving but remained high, with deficit rates of -157.3%, -135.8% and -126.0% in 2020, 2021 and 2022, respectively. Xinyi's government fund income, mainly generated by land sales, increased to c. RMB6.3 billion in 2022 from RMB5.1 billion in 2021. Plus, the transfer payment from higher governments was largely stable. Therefore, the Xinyi government's aggregate revenue reached RMB16 billion in 2022, up from RMB14.1 billion in 2021.

Nevertheless, the outstanding debt of the Xinyi government continued to grow in 2022. At end-2022, the Xinyi government's outstanding debt was RMB17.0 billion (end-2021: RMB13.5 billion). Given that the Xinyi government borrowed heavily in special debts to support its public projects, its fiscal debt ratio, as measured by total government debt outstanding/aggregate revenue, had increased to 106.5% at end-2022 from 95.7% at end-2021.

XHCD's Financial and Liquidity Position: XHCD's asset size grew significantly to RMB40.1 billion at end-2022 from RMB22.5 billion at end-2020, mainly due to the multiple asset injections from the local government. The company's debt was largely stable in the past three years, which was RMB6.6 billion, 7.6 and 7.7 billion in 2020, 2021 and 2022, respectively. Therefore, XHCD's financial leverage, as measured by total debt/capitalization, decreased to 19.9% in 2022, a relatively healthy level, from 29.3% in 2020.

XHCD's liquidity was very tight. At end-2022, XHCD held a cash balance of RMB543 million (including restricted cash of RMB511 million), while its debts due within one year amounted to RMB3.2 billion. The company had only RMB1.1 billion in unused bank credit lines to support its debt repayments and business operations. Consequently, XHCD needs to successfully roll over its short-term bank borrowings and secure additional financing sources or government support to maintain its liquidity.

Rating Sensitivities

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

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

Operating Environment

Economic Condition of Xinyi

Xinyi is a county-level city directly under the jurisdiction of Jiangsu Province and managed by Xuzhou. Xinyi has jurisdiction over 13 towns, 5 streets, and 2 provincial-level development zone (High-tech Zone and Xinyi economic development zone). At end-2022, Xinyi had a total area of 1,616 square kilometers and a resident population of 0.96 million, with an urbanization rate of 58.0%.

Xinyi's GDP growth rate fluctuated in the past three years, owing to Covid's disruption, which was 3.1%, 10.1% and 4.7% in 2020, 2021 and 2022, respectively. It realized a GDP of RMB82.6 billion in 2022, and was ranked 4th among ten districts and counties under the administration of Xuzhou. In recent years, Xinyi's economic development focused on manufacturing, biological, pharmaceutical and chemical industries. Its economic growth was mainly fueled by the secondary and tertiary sectors, which accounted for 39.0% and 49.3% of GDP in 2022, respectively.

Xinyi's GDP and Fixed Asset Investment

(RMB billion)	2020	2021	2022
GDP	69.2	78.1	82.6
-Primary industry (%)	13.0	11.9	11.7
-Secondary industry (%)	38.3	38.1	39.0
-Tertiary industry (%)	48.7	50.0	49.3
GDP growth rate (%)	3.1	10.1	4.7
Fixed asset investment growth rate (%)	5.3	8.7	3.1
Population (million)	0.92	0.96	0.96

Source: Public information and Lianhe Global's calculations

Fiscal Condition of Xinyi

The Xinyi government's budgetary revenue increased to RMB4.6 billion in 2022 from RMB3.8 billion in 2020. However, the tax revenue's contribution decreased to 70.7% from 85.9% over the same period. Xinyi's budgetary deficit was improving but remained high, with deficit rates of -157.3%, -135.8% and -126.0% in 2020, 2021 and 2022, respectively. Xinyi's government fund income, mainly generated by land sales, increased to c. RMB6.3 billion in 2022, with a year-on-year growth rate of 24.4%. Plus, the transfer payment from higher governments was largely stable. Therefore, the Xinyi government's aggregate revenue reached RMB16 billion in 2022, up from RMB14.1 billion in 2021.

Nevertheless, the outstanding debt of the Xinyi government continued to grow in 2022. At end-2022, the Xinyi government's outstanding debt was RMB17.0 billion (end-2021: RMB13.5 billion), including general obligations of RMB2.9 billion and special debt of RMB14.1 billion. Given that the Xinyi government borrowed heavily in special debts to support its public projects, its fiscal debt ratio, as

measured by total government debt outstanding/aggregate revenue, had increased to 106.5% at end-2022 from 95.7% at end-2021.

Xinyi's Fiscal Condition			
(RMB billion)	2020	2021	2022
Budgetary revenue	3.8	4.4	4.6
Budgetary revenue growth rate (%)	5.5	16.6	10.6*
Tax revenue	3.2	3.7	3.3
Tax revenue (% of budgetary revenue)	85.9	84.4	70.7
Government fund income	4.9	5.1	6.3
Transfer payment	5.0	4.7	5.1
Aggregate revenue	13.7	14.1	16.0
Budgetary expenditure	9.6	10.3	10.4
Budget deficit ¹ (%)	-157.3	-135.8	-126.0

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

Source: Public information and Lianhe Global's calculations

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

Ownership Structure

Full Government Ownership

XHCD was established in September 2016 by the Xinyi government. At end-2022, the Xinyi government, as the sole controlling shareholder, held 100% equity of the XHCD and entrusted the company's management to Xiyi High-tech Industrial Development Zone Management Committee ("XHZ MC").

Strategic Importance and Government Linkage

Strategic Importance of XHCD to Xinyi

XHCD's strategic development plan has been aligned with the local government's economic and social policies. It is the key LIDC responsible for project construction, including land development, infrastructure construction and urban village renovation, in High-tech Zone, a provincial-level development zone focusing on the electronic information, machinery manufacturing, biopharmaceuticals, light textile, and logistics processing industry. The company also develops and operates industrial parks in High-tech Zone to promote Xinyi's industrial and economic development.

Linkage with the Local Government

XHCD has a strong linkage with the local government. Xinyi government holds 100% shares of XHCD directly. The local government has strong control over the company, including the appointment of senior management and supervision of development strategy, major financing plan and investment decisions. In addition, the local government has formulated a performance assessment policy for the company, and regularly appoints auditors to review the company's operating performance and financial position.

Ongoing Government Support

The company received ongoing operational subsidies from the Xinyi government in relation to providing public services. In addition, XHCD received multiple capital

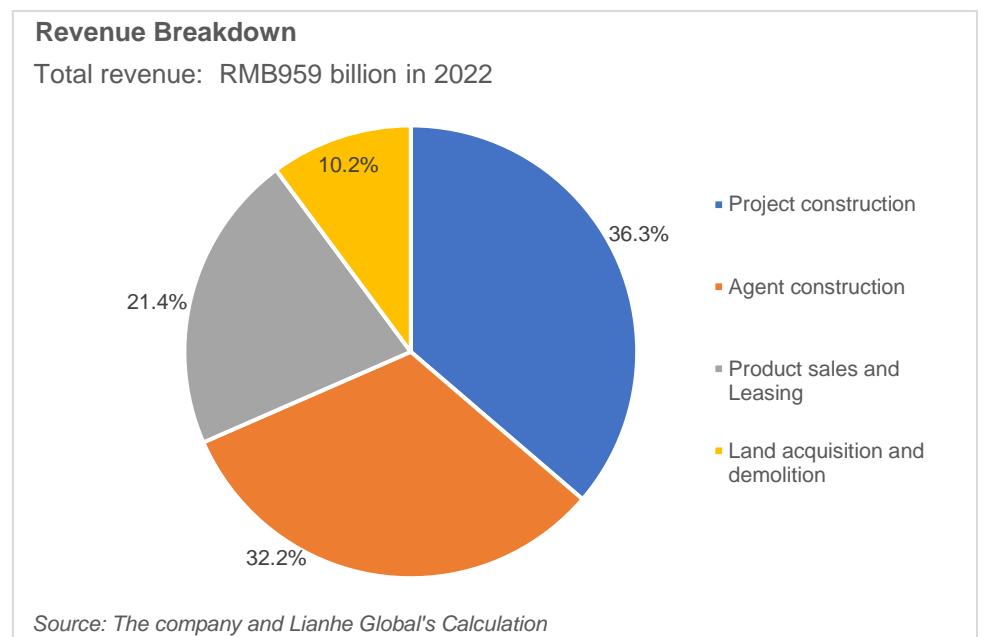
injections, including cash, completed projects and lands, etc., over the same period. Considering its strategic importance in Xinyi, we expect the company to continue receiving government support in the future.

Business Profile

The Key Entity Responsible for Project Construction in High-tech Zone

XHCD is an important LIDC in Xinyi responsible for land development, infrastructure construction, urban village renovation, industrial parks development, and operation in High-tech Zone. As the core platform designated by the XHZ MC to implement its infrastructure construction plans, XHCD plays a crucial role in promoting economic and social development in the region.

XHCD's primary source of revenue was project construction activities, while it also engaged in commodity sales and leasing businesses. The company realized revenue of RMB803 million, 907 million, and 959 million in 2020, 2021 and 2022, respectively, demonstrating a steady growth trend. The company's gross profit margin remained stable at c. 16% over the same period.



Project Construction, Agent Construction, and Land Acquisition and Demolition

XHCD undertakes an array of projects, including land acquisition and demolition, construction of roads, industrial parks, public facilities and resettlement houses in High-tech Zone entrusted by XHZ MC. XHCD usually recognizes construction costs incurred plus an additional margin of 15%-20% as revenue annually. However, the cash collection could be subject to project and payment delays.

XHCD boasts an extensive project pipeline, although it may also result in substantial capital expenditure pressure. At end-2022, XHCD had ten projects

underway, with a total planned investment of RMB2.5 billion. Of this amount, RMB472 million is to be invested within the next one to two years.

Product sales and Leasing

XHCD also involves in the sales of cotton and linen, aluminum and chemical products. Other businesses of the company include property lease and management. They mainly supplement and diversify the company's revenue and have a relatively small impact on XHCD's financial position and creditworthiness.

Financial Profile

Balance Sheet Structure and Quality

Balance Sheet Structure and Quality

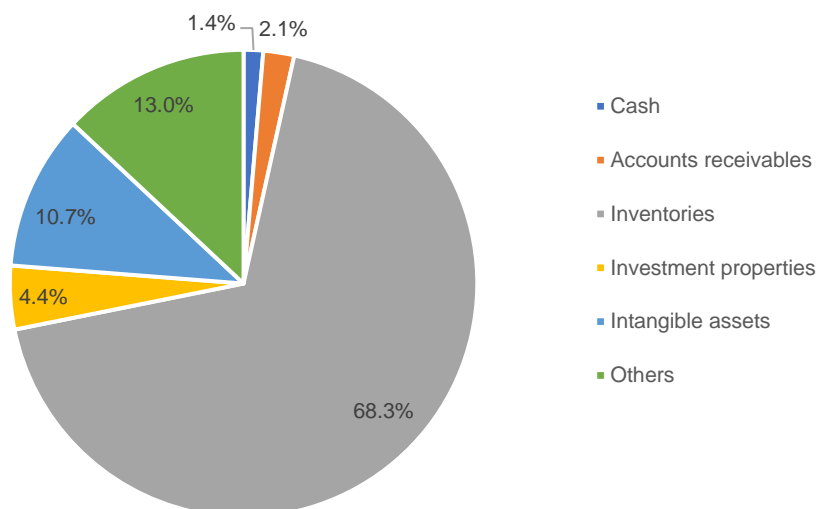
(RMB million)	2020	2021	2022
Total Asset	22,528	34,741	40,081
Equity	15,867	26,744	30,835
Debt	6,562	7,600	7,660
Debt / (Debt + Equity) (%)	29.3	22.1	19.9
LT Debt	4,692	4,978	4,473
LT Debt / (LT Debt + Equity) (%)	22.8	15.7	12.7

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

XHCD's asset size grew significantly to RMB40.1 billion at end-2022 from RMB22.5 billion at end-2020, mainly due to the multiple asset injections from the local government. The company's debt was largely stable in the past three years, which was RMB6.6 billion, 7.6 and 7.7 billion in 2020, 2021 and 2022, respectively. Therefore, XHCD's financial leverage, as measured by total debt /capitalization, decreased to 19.9% in 2022, a relatively healthy level, from 29.3% in 2020.

Asset Breakdown

(Total asset: RMB40.1 billion at end-2022)



Source: The company and Lianhe Global's calculation



XHCD's asset liquidity was weak. The company's active involvement in the High-tech Zone's land development and project construction activities led to the accumulation of substantial construction costs recorded in inventories, and accounts receivable, totaling RMB15.2 billion and RMB856 million at the end-2022, respectively. Given the lengthy construction, recognition, and cash collection processes, these assets typically require an extended period to monetize.

XHCD also recorded lands to be developed of RMB12.2 billion in its inventories and land use rights of RMB4.3 billion as intangible assets, both mainly injected by the local government. Additionally, XHCD held RMB1.8 billion in investment properties at the end of 2022, primarily consisting of self-operated industrial park projects for leasing. However, these properties generated only RMB2.6 million in leasing income in 2022. We believe that the liquidity of XHCD's lands and properties is highly dependent on property market conditions and is weakened by the fact that a significant portion of these assets has been pledged to secure bank borrowings.

At end-2022, XHCD's other assets mainly consisted of other receivables of RMB1.5 billion (mainly due from government agencies and LIDCs in Xinyi), and debt investments in Xinyi's other LIDCs totaling RMB2.1 billion. Yet they usually do not have specified repayment plans.

Debt Servicing Capability

XHCD's liquidity was very tight. At end-2022, XHCD held a cash balance of RMB543 million (including restricted cash of RMB511 million), while its debts due within one year amounted to RMB3.2 billion. The company had only RMB1.1 billion in unused bank credit lines to support its debt repayments and business operations. Consequently, XHCD needs to successfully roll over its short-term bank borrowings and secure additional financing sources or government support to maintain its liquidity.

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