

Feicheng City Assets Management Group Co., Ltd.

Initial Issuer Report

Summary

Issuer Rating	BBB
Outlook	Stable
Location	China
Industry	Local Investment and Development Companies
Date	19 June 2023

Key Figures of Feicheng and FCAMG (RMB billion)

	2021	2022
Feicheng		
GDP	77.1	82.7
GDP growth rate (%)	4.7	5.3
Budgetary revenue	4.5	4.7
Government fund	2.1	1.6
Transfer payment	2.0	2.3
Budgetary expenditure	5.9	6.9
FCAMG	2021	2022
Assets	16.5	19.2
Equity	12.5	12.8
Revenue	0.6	1.3

Source: Public information, FCAMG 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 Feicheng City Assets Management Group Co., Ltd. (“FCAMG” or “the company”)

Summary

The Issuer Credit Rating reflects a high possibility that the People’s Government of Feicheng City, Taian City (“Feicheng government”) would provide very strong support to FCAMG if needed, in light of its indirect full ownership of FCAMG, FCAMG’s strategic importance as the important local investment and development company (“LIDC”) that is responsible for major infrastructure construction and water operation in Feicheng City, Taian City (“Feicheng”), (“Taian”), and the linkage between the Feicheng government and FCAMG, 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 Feicheng government may face significant negative impact on its reputation and financing activities if FCAMG encounters any operational and financial difficulties.

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

Rating Rationale

Feicheng Government’s Ownership and Supervision: The Feicheng government indirectly holds the full 100% ownership of FCAMG via the State-owned Assets Operation Centre of Feicheng (“Feicheng SAOC”), and is the actual controller of the company. The Feicheng 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 Feicheng government has assessment mechanism over the company and appoints auditor to supervise the operating performance and financial position on a periodic basis.

Strategic Importance to Feicheng and Strategic Alignment: FCAMG is an important infrastructure construction and water operation entity within the region. FCAMG plays an important role in promoting the economic and social development of the region. Its business operation and development have been aligned with the government’s development plans.

Ongoing Government Support: FCAMG received operational and financial support from the government. FCAMG received a total subsidy amount of c. RMB781.1 million from 2020 to 2022. Given the franchised advantages in water operation in Feicheng, we believe FCAMG is likely going to receive government support in the form of operational and/or financial subsidies to support its daily business operation.

FCAMG’s Financial Matrix and Liquidity Position: FCAMG’s total assets showed a continuous growth in the past few years, with a growth rate of 18.6% and 16.5% at end-2021 and end-2022, respectively, and reached RMB19.2 billion at end-2022. The increase of FCAMG’s total assets in 2022 was largely due to its inventories, which has steadily increased in tandem with the company’s infrastructure construction projects. Though FCAMG had large proportion of current assets (79.1% at end-2022), its assets were illiquid,

Analysts

Ben Yau
 +852 3462 9586
ben.yau@lhratingsglobal.com

Toni Ho
 (852) 3462 9578
toni.ho@lhratingsglobal.com

Applicable Criteria

[China Local Investment and Development Companies Criteria \(5 December 2022\)](#)

primarily due to the significant proportion of land reserves, costs associated with construction projects and receivables. FCAMG's financial leverage (total liabilities to assets) was 33.1% at end-2022. FCAMG's total adjusted debt increased to c. RMB4.5 billion at end-2022. The liquidity of FCAMG was tight. At end-2022, FCAMG had unrestricted cash balance and unused credit facilities of c. RMB0.25 billion and RMB1.0 billion, respectively, compared with its debt due within one year of c. RMB1.5 billion at the same time. However, FCAMG has access to various financing channels, including bank loans, bond issuance and non-traditional financing, to support its debt repayment and business operations.

Economy and Fiscal Condition of Feicheng: Feicheng is a county-level city of Taian, Shandong Province and is located in the northwest of Taian with a total land area of c.1,277 square kilometers. Feicheng maintained steady economic growth in the recent three years. Its GDP reached c. RMB82.7 billion in 2022, representing a year-on-year growth rate of 5.3%. Feicheng's GDP amount was ranked 1st out of all cities, districts and counties of Taian in 2022. The aggregate fiscal revenue of the Feicheng government was mainly derived from the budgetary revenue and transfer payment. The budgetary revenue of the Feicheng government maintained steady growth in the past three years, and reached RMB4.7 billion in 2022. The tax revenue accounted for 81.8%-86.1% of the budgetary revenue from 2020 to 2022. The debt ratio, as measured by the total government debt/aggregate revenue was lifted to 88.1% in 2022 from 56.0% in 2020, mainly due to the increase in special debt.

Rating Sensitivities

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

We would consider upgrading FCAMG's rating if there is an upgrade in our internal credit assessment on the Feicheng government.

Operating Environment

Economic Condition of Feicheng

Feicheng is a county-level city of Taian City, Shandong Province and is located in the northwest of Taian. Feicheng is a time-honored city with abundant tourism resources and cultural sites. Feicheng has jurisdiction over 10 towns, 4 streets, 1 national high-tech development zone and 1 provincial-level economic development zone with a total land area of c.1,277 square kilometers. By the end of 2021, Feicheng had a resident population of c. 0.9 million, with an urbanization rate of 68.1%.

Feicheng maintained steady economic growth in the recent three years. Its GDP reached c. RMB82.7 billion in 2022, representing a year-on-year growth rate of 5.3%. Feicheng's GDP amount was ranked 1st out of all cities, districts and counties of Taian in 2022. The economic growth of Feicheng was mainly boosted by the secondary and tertiary industries, which accounted for 51.5% and 40.5% of GDP in 2022, respectively. The fixed asset investment turned to increase in 2022 after two years decrease and achieved RMB20.3 billion in 2022.

Feicheng's GDP and Fixed Asset Investment			
(RMB billion)	2020	2021	2022
GDP	72.2	77.1	82.7
-Primary industry (%)	7.9	8.1	8.0
-Secondary industry (%)	50.0	49.3	51.5
-Tertiary industry (%)	42.1	42.6	40.5
GDP growth rate (%)	3.5	4.7	5.3
Fixed asset investment	46.5	29.1	35.5
Fixed asset investment growth rate (%)	-16.3	-37.3	21.9
Population (million)	0.9	0.9	0.9

Source: Public information, the company and Lianhe Global's calculations

Fiscal Condition of Feicheng

The aggregate fiscal revenue of the Feicheng government was mainly derived from the budgetary revenue and transfer payment. The budgetary revenue of the Feicheng government maintained steady growth in the past three years, and reached RMB4.7 billion in 2022. The tax revenue accounted for 81.8%-86.1% of the budgetary revenue from 2020 to 2022. The financial self-sufficiency rate of Feicheng was insufficient.

The outstanding debt of the Feicheng government showed an upward trend in recent years and reached c. RMB8.1 billion at end-2022, which included RMB2.6 billion general obligations and RMB5.5 billion special debt. The debt ratio, as measured by the total government debt/aggregate revenue was lifted to 88.1% in 2022 from 56.0% in 2020, mainly due to the increase in special debt.

Feicheng's Fiscal Condition			
(RMB billion)	2020	2021	2022
Budgetary revenue	4.1	4.5	4.7
Budgetary revenue growth rate (%)	1.1	9.4	14.9*
Tax revenue	3.5	3.8	3.8
Tax revenue (% of budgetary revenue)	86.1	85.7	81.8
Government fund income	3.3	2.1	1.6
Transfer payment	2.0	2.0	2.3
Aggregate revenue	9.4	8.7	9.2
Budgetary expenditure	6.1	5.9	6.9
Budget deficit ¹ (%)	-48.4	-32.7	-47.6

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

*Excluding the influence of value-added tax credit refund

Source: Public information and Lianhe Global's calculations

Ownership Structure

Government's Ownership

FCAMG was established with the approval of the Feicheng government in January 2003, with an initial registered capital of RMB100 million. After an array of capital injections, at end-2022, FCAMG's registered capital was RMB2 billion and the paid-in capital was RMB458.1 million. As of June 9, 2023, The Feicheng SAOC holds 40% shares of FCAMG through Feicheng City Construction Investment Group Co., Ltd. ("FCCIG"), whose parent company is Feicheng Urban Investment Control Group Co., LTD., which is wholly owned by The Feicheng SAOC. The Feicheng SAOC also holds 60% shares of FCAMG through Feicheng Urban Assets Holding Group Co., LTD. The Feicheng government via the Feicheng SAOC indirectly holds 100% ownership of FCAMG and is the ultimate controller of the company.



Strategic Importance and Government Linkage

Strategic Importance of FCAMG to Feicheng

FCAMG is an important infrastructure construction and water operation entity within the region. FCAMG plays an important role in promoting the economic and social development of the region. Its business operation and development have been aligned with the government's development plans.

Strong Linkage with the Local Government

The Feicheng government indirectly holds the full 100% ownership of FCAMG via Feicheng SAOC, and is the actual controller of the company. The Feicheng 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 Feicheng government has assessment mechanism over the company and appoints auditor to supervise the operating performance and financial position on a periodic basis.

Government Support

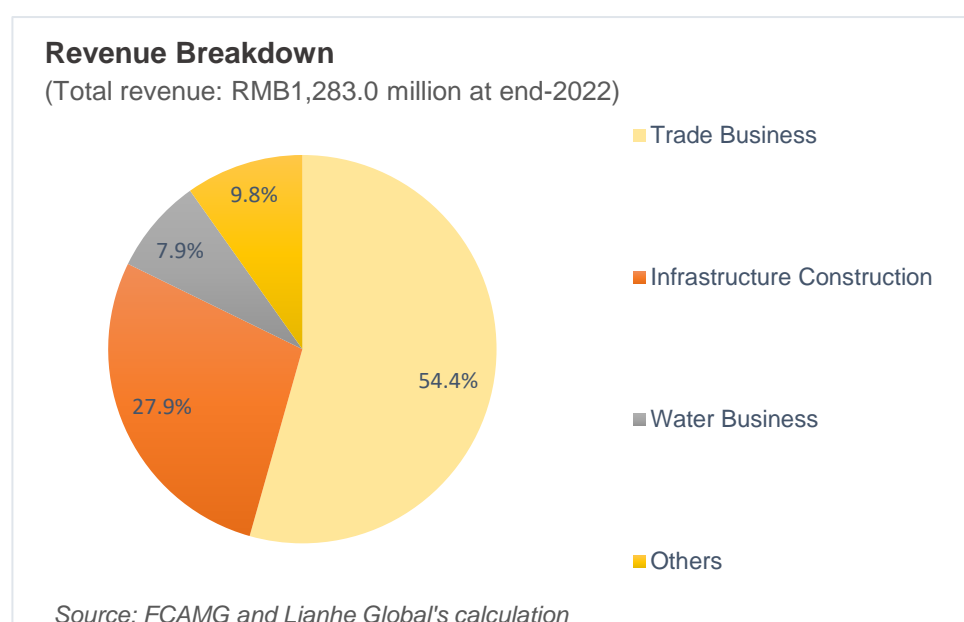
FCAMG continued to receive financial subsidies, mainly including operating subsidies, from the local government to maintain its business operation. FCAMG received subsidies of c. RMB162.3 million, RMB244.7 million and RMB374.1 million in 2020, 2021 and 2022, respectively. Given the franchised advantages in water operation in Feicheng, we believe FCAMG 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 important Entity Responsible for Infrastructure Construction and Water Operation Entity in Feicheng

As an important LIDC in Feicheng, the FCAMG's business is mainly focused on infrastructure construction, water operation, pipe network leasing, trade and other businesses. Benefiting from sufficient projects and regional franchise in water business, the company enjoys good business continuity with steady cash flow.

The main sources of operating revenue for FCAMG are infrastructure construction, water operation and trading business, while it is also engaged in pipe network leasing, quarantine testing, public transport operation and property services. The company's total revenue realized RMB398.7 million, RMB593.6 million and RMB1.3 billion in 2020, 2021 and 2022, respectively, representing an upward trend. Meanwhile, the overall gross profit margin of FCAMG decreased to 7.8% in 2022 from 14.8% in 2020.



Infrastructure Construction

FCAMG's infrastructure construction business mainly adopts agent construction model and bidding model. Under the agent construction mode, the company is entrusted by the Feicheng government to undertake the construction of infrastructure projects. The company signs construction agreements with the Feicheng government and the Feicheng Finance Bureau ("FFB") and receives a construction fee of 9% of the actual expense of the construction projects as revenue. Under the bidding model, the business is mainly handled by its subsidiary Feicheng Luxing Construction Co., Ltd. ("FLC"), which bids for construction projects through market-based bidding. After winning the bids, FLC is responsible for the construction of projects and will recognize revenue at the end of each year in accordance with the construction contracts. FCAMG's infrastructure construction income reached RMB237.0 million, RMB427.6 million and RMB357.4 million in 2020, 2021 and 2022, respectively. The gross profit margin of FCAMG's infrastructure business was on an upward trend, increasing from 8.6% in 2020 to 17.2% in 2022. Currently, the company is working on several large-scale projects, thus it incurs high capital expenditure pressure.

Water Business

FCAMG's water business includes water supply and sewage treatment with regional advantages. The water supply business is handled by subsidiary Feicheng Water Group Co., Ltd. ("FWG"), the water source is raw water provided by the government at no cost. The tap water and industrial water are sold through the integrated pipeline network. The sewage treatment business is also controlled by FWG, which is responsible for the operation of the sewage treatment plant, and the government pays for it based on the sewage treatment fees charged to end-users.

Trading Business

FCAMG diversified its business operations in 2022 by adding the trading business to complement its main operations. This segment is primarily handled by its subsidiary, Shandong Sanliujiu Smart Supply Chain Management Co., Ltd. The company's trading business is mainly engaged in the sales of steel and mostly conducted in a "demand-driven" model, where it determines the amount of materials to be procured strictly based on the actual purchase orders placed by customers. The company makes a profit from the spread between buying and selling prices. The income generated from this segment reached RMB0.7 billion in 2022, with a gross profit margin of 2.3%. In addition, CTDCE also added the production and sales business of pharmaceutical glass tube. The pharmaceutical glass tube adopts the ordering production and sales mode, with borax from the United States and quartz sand from Fengyang region as the main raw materials. Generally, the settlement will be made in cash or bank acceptance two months after the invoice is issued.

Other Businesses

Other businesses of the company include pipe network leasing, quarantine testing, public transport operation and property services, etc., with each segment accounted for a relatively small proportion of the company's total revenue. Other businesses mainly play the role of supplementing the revenue of the main business and make the revenue structure more diversified.

Financial Profile

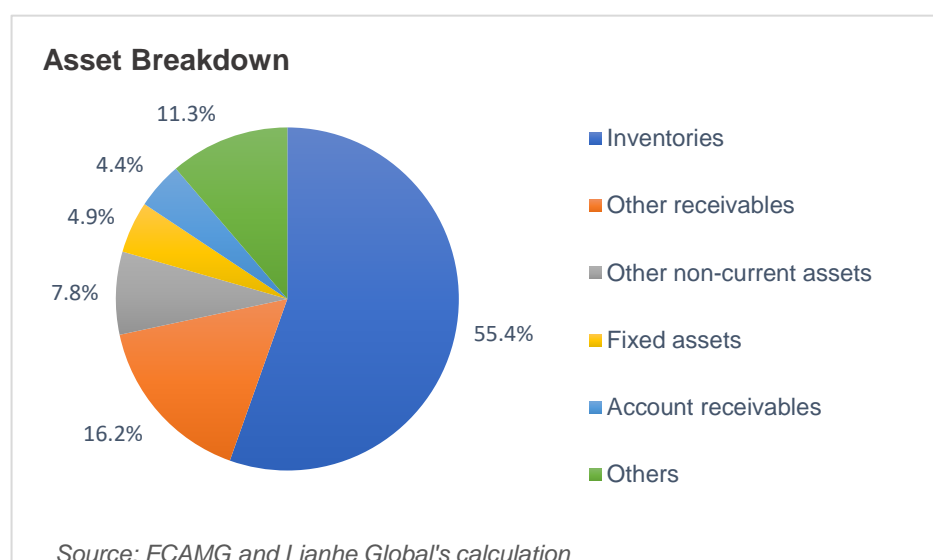
Balance Sheet Structure and Quality

Balance Sheet Structure and Quality			
(RMB million)	2020	2021	2022
Total Asset	13,889	16,478	19,190
Equity	12,091	12,536	12,841
Debt	1,350	2,752	4,524
Debt / (Debt + Equity) (%)	10.0	18.0	26.1
LT Debt	574	1,455	3,008
LT Debt / (LT Debt + Equity) (%)	4.5	10.4	19.0

Source: Company information and Lianhe Global's calculations

FCAMG's total assets showed a continuous growth in the past few years, with a growth rate of 18.6% and 16.5% at end-2021 and end-2022, respectively, and reached RMB19.2 billion at end-2022. The increase of FCAMG's total assets in 2022 was largely due to its inventories, which has steadily increased in tandem with the company's infrastructure construction projects. FCAMG's assets mainly consisted of inventories, other receivables, other non-

current assets, fixed assets and account receivables. Inventories mainly included land reserves, mainly government land reserves and allocated land for commercial and residential use, and construction costs of infrastructure projects. Other receivables and account receivables were mainly transactions with the Feicheng FFB, other state-owned enterprises and other government agencies in Feicheng, which had an aging period of mostly 1-3 years, with controllable counterparty risk and low bad debt provision. Other non-current assets were advance payment for construction or land, etc. Fixed assets primarily consisted of pipeline networks and structures. Though FCAMG had large proportion of current assets (79.1% at end-2022), its assets were illiquid, primarily due to the significant proportion of land reserves, costs associated with construction projects and receivables.



FCAMG's financial leverage (total liabilities to assets) reached 13.0%, 23.9% and 33.1% at end-2020, end-2021 and end-2022, respectively, representing an upward trend due to the increasing Long-term payable. FCAMG's total adjusted debt increased by 235.0% from c. RMB1.4 billion at end-2020 to c. RMB4.5 billion at end-2022, with short-term debt and long-term debt accounting for c. 33.5% and c. 66.5% of the total debt. There was no significant change in the ownership equity structure of FCAMG at end-2022, compared with that at end-2020. FCAMG mainly relies on external financing to support its capital expenditures and debt repayment, which we expect to increase in the future given its infrastructure related projects under construction and to be constructed in the future.

Debt Servicing Capability

The liquidity of FCAMG was tight. At end-2022, FCAMG had unrestricted cash balance and unused credit facilities of c. RMB0.25 billion and RMB1.0 billion, respectively, compared with its debt due within one year of c. RMB1.5 billion at the same time. However, FCAMG has access to various financing channels, including bank loans, bond issuance and non-traditional financing, to support its debt repayment and business operations.

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