

## Pizhou Communications Holding Group Co., Ltd.

### Initial Issuer Report

#### Summary

Issuer Rating	BBB-
Outlook	Stable
Location	China
Industry	Local Investment and Development Companies
Date	30 June 2023

#### Key Figures of Pizhou and PCHG (RMB billion)

	2021	2022
<b>Pizhou</b>		
GDP	110.8	115.7
GDP growth rate (%)	9.5	4.2
Budgetary revenue	4.7	4.3
Government fund	14.6	10.7
Transfer payment	6.2	6.6
Budgetary expenditure	12.7	12.5
<b>PCHG</b>	<b>2021</b>	<b>2022</b>
Assets	12.3	14.5
Equity	7.2	7.4
Revenue	0.6	0.7

Source: Public information, PCHG 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 Pizhou Communications Holding Group Co., Ltd. ("PCHG" or "the company")

#### Summary

The Issuer Credit Rating reflects a high possibility that the People's Government of Pizhou City, Xuzhou City ("Pizhou government") would provide strong support to PCHG if needed, in light of its full ownership of PCHG, PCHG's strategic importance as the important local investment and development company ("LIDC") that is responsible for transportation-related facilities construction and operation in Pizhou City, Xuzhou City ("Pizhou"), and the linkage between the Pizhou government and PCHG, 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 Pizhou government may face significant negative impact on its reputation and financing activities if PCHG encounters any operational and financial difficulties.

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

#### Rating Rationale

**Pizhou Government's Ownership and Supervision:** The Pizhou government holds the full ownership of PCHG through Pizhou Finance Bureau. The Pizhou 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 Pizhou 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 Pizhou and Strategic Alignment:** PCHG is primarily responsible for transportation-related facilities construction and operation within the region. PCHG 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:** PCHG received operational and financial support from the government. PCHG received a total subsidy amount of c. RMB427 million from 2020 to 2022, mainly including operating subsidies. We believe PCHG is likely going to receive government support in the form of operational and/or financial subsidies to support its daily business operation.

**PCHG's Financial Matrix and Liquidity Position:** PCHG's total assets showed a continuous growth in the past few years, with a growth rate of 16.4% and 17.1% at end-2021 and end-2022, respectively, and reached RMB14.5 billion at end-2022. The increase of PCHG's total assets in 2022 was largely due to its inventories and other receivables. Although the company's asset structure was dominated by current assets, the inventories monetization was heavily influenced by the progress of government settlements, the use of some assets was restricted and some funds were occupied by accounts receivable. Therefore, the company's overall asset liquidity was weak. PCHG's financial leverage (total

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#### Applicable Criteria

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

liabilities to assets) reached 35.5%, 41.8% and 48.9% at end-2020, end-2021 and end-2022, respectively, representing an upward trend. PCHG's total adjusted debt increased to c. RMB5.4 billion at end-2022. The liquidity of PCHG was tight. At end-2022, PCHG had unrestricted cash balance and unused credit facilities of c. RMB0.1 billion and RMB2.1 billion, respectively, compared with its debt due within one year of c. RMB3.3 billion at the same time. Therefore, the company needs to roll over its short-term bank borrowings (end-2022: c. RMB2.6 billion). In addition, obtaining additional financing sources or government support are also important to the company in maintaining its liquidity.

**Economy and Fiscal Condition of Pizhou:** Pizhou is a county-level city directly under the jurisdiction of Jiangsu Province and managed by Xuzhou City on behalf of Jiangsu Province, and located in the northernmost of Jiangsu Province. Pizhou ranked 45<sup>th</sup> among the China's top 100 counties in terms of comprehensive strength in 2022, with its GDP recording at c. RMB115.7 billion, representing a year-over-year growth rate of 4.2%. The Pizhou government's aggregate fiscal revenues are mainly derived from government fund income. The Pizhou government's budgetary revenue reached c. RMB4.3 billion in 2022, with the tax revenue accounting for 74.4% of its budgetary revenue. In addition, Pizhou's government fund income, mainly generated by land sales, dropped by 26.9% to c. RMB10.7 billion in 2022, owing to the weak property market. Its fiscal debt ratio, as measured by total government debt outstanding/aggregate revenue, had increased to 79.2% at end-2022 from 70.1% at end-2020, mainly due to the increase in special debt.

### Rating Sensitivities

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

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

### Operating Environment

#### Economic Condition of Pizhou

Pizhou is a county-level city directly under the jurisdiction of Jiangsu Province and managed by Xuzhou City on behalf of Jiangsu Province, and located in the northernmost of Jiangsu Province. Pizhou has jurisdiction over 21 towns, 4 streets and 2 provincial economic development zones, with a total area of 2,088 square kilometers. At end-2021, Pizhou had a resident population of c. 1.4 million, making it the second populous county in Jiangsu Province, with an urbanization rate of 58.8%.

Pizhou ranked 45<sup>th</sup> among the China's top 100 counties in terms of comprehensive strength in 2022, with its GDP recording at c. RMB115.7 billion, representing a year-over-year growth rate of 4.2%. Pizhou's economic growth was mainly fueled by the secondary and tertiary industries in the past few years, which accounted for 39.1% and 46.1% in 2022, respectively. Its economic development focused on semiconductors, carbon-based new materials industry and high-end equipment manufacturing in recent years.

**Pizhou's GDP and Fixed Asset Investment**

(RMB billion)	2020	2021	2022
GDP	100.1	110.8	115.7
-Primary industry (%)	15.9	14.9	14.9
-Secondary industry (%)	39.6	40.1	39.1
-Tertiary industry (%)	44.5	45.0	46.1
GDP growth rate (%)	3.9	9.5	4.2
Fixed asset investment	49.7	54.0	55.7
Fixed asset investment growth rate (%)	5.3	8.5	3.3

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

## Fiscal Condition of Pizhou

The Pizhou government's aggregate fiscal revenues are mainly derived from government fund income. The Pizhou government's budgetary revenue reached c. RMB4.3 billion in 2022, with the tax revenue accounting for 74.4% of its budgetary revenue. The fiscal self-sufficiency rate of the Pizhou government was insufficient, and it recorded budget deficit of -189.6% in 2022. In addition, Pizhou's government fund income, mainly generated by land sales, dropped by 26.9% to c. RMB10.7 billion in 2022, owing to the weak property market.

The outstanding debt of the Pizhou government continued to grow. At end-2022, the Pizhou government's outstanding debt was c. RMB17.1 billion, including RMB3.9 billion of general obligations and RMB13.2 billion of special debt. Its fiscal debt ratio, as measured by total government debt outstanding/aggregate revenue, had increased to 79.2% at end-2022 from 70.1% at end-2020, mainly due to the increase in special debt.

**Pizhou's Fiscal Condition**

(RMB billion)	2020	2021	2022
Budgetary revenue	4.4	4.7	4.3
Budgetary revenue growth rate (%)	2.5	7.8	1.9*
Tax revenue	3.5	3.8	3.2
Tax revenue (% of budgetary revenue)	80.6	80.2	74.4
Government fund income	8.1	14.6	10.7
Transfer payment	7.1	6.2	6.6
<b>Aggregate revenue</b>	<b>19.6</b>	<b>25.6</b>	<b>21.6</b>
Budgetary expenditure	12.6	12.7	12.5
Budget deficit <sup>1</sup> (%)	-187.6	-168.4	-189.6

<sup>1</sup> 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

PCHG was established in October 2019 with an initial registered capital of RMB0.2 billion, funded by Pizhou Finance Bureau. In December 2019, Pizhou Finance Bureau, as sole shareholder of the company, increased the registered capital of the company to RMB0.6 billion in monetary form.

At end-2022, the registered and paid-in capital of the company was both RMB0.6 billion. Pizhou Finance Bureau remains as the sole shareholder of the company. The actual controller of the company is the Pizhou government.

## Strategic Importance and Government Linkage

### Strategic Importance of PCHG to Pizhou

PCHG is primarily responsible for transportation-related facilities construction and operation within the region. PCHG 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 Pizhou government holds the full ownership of PCHG through Pizhou Finance Bureau. The Pizhou 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 Pizhou government has assessment mechanism over the company and appoints auditor to supervise the operating performance and financial position on a periodic basis.

### Government Support

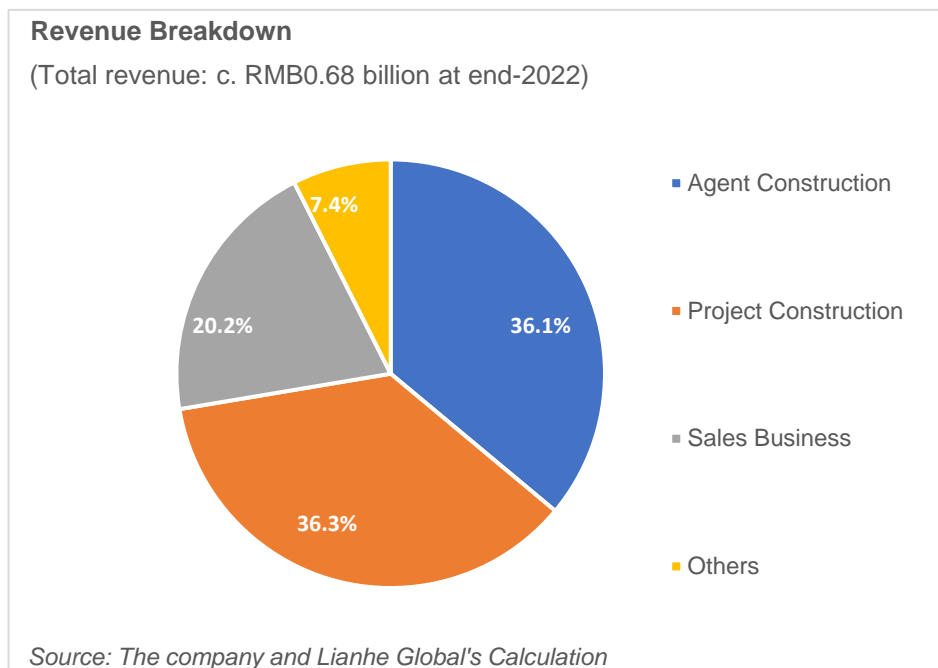
PCHG continued to receive financial subsidies, mainly including operating subsidies, from the local government to maintain its business operation. PCHG received subsidies of c. RMB124 million, RMB145 million and RMB158 million in 2020, 2021 and 2022, respectively. We believe PCHG is likely going to receive government support in the form of operational and/or financial subsidies to support its daily business operation.

## Business Profile

### The Important Entity Responsible for Transportation-related Facilities Construction in Pizhou

PCHG, as an important LIDC in Pizhou, is mainly responsible for investment, construction, development and operation of transportation facilities in Pizhou, as well as the expansion of transportation-related industries. As the core platform for the construction of government-commissioned transportation facilities in Pizhou, the company has played an important role in promoting the economic and social development of the region. According to the management of the company, under the background of Pizhou's current external initiative to connect with the "Belt and Road" and its inner plate consciously integrating into the "Huaihai Economic Zone", there will be an increasing demand for high-level integrated transportation hubs in the future. Therefore, PCHG is expected to obtain more projects to expand its assets and revenue scale.

The primary sources of operating revenue for PCHG are agent construction, engineering construction and sales business, while it also engaged in road tolling, passenger transport and leasing, etc. The company's total revenue reached c. RMB0.6 billion, RMB0.6 billion and RMB0.7 billion in 2020, 2021 and 2022, respectively, representing an upward trend. The overall gross profit margin of PCHG remained stable at c. 5%-9% from 2020 to 2022. In general, PCHG's business was relatively concentrated, and it has regional advantages in its major businesses.



### Agent Construction

PCHG is designated by the Pizhou government to undertake the transportation-related facilities construction business within the region (excluding High-tech Zone and Development Zone). The projects in this segment are generally conducted under the agent construction model. The company has entered into an agreement with the Pizhou Municipal Transportation Bureau, which provides that upon completion and acceptance of the project both parties will add 20% to the actual cost of the project as the final settlement price, so as to form the company's receivables to the client. The entrusting party pays the issuer settlement amounts gradually from time to time. The projects were mainly financed by the company's own funds and external financing. Currently, the company's projects under construction and to be constructed still require a large scale of investment, thus it incurs high pressure on capital expenditure.

### Project Construction

The company obtained projects through public bidding, which mainly included subcontracting projects from the Pizhou Municipal Bureau of Transportation and the Xuzhou Municipal Highway Management Department. For undertaking construction projects, the owner signs a relevant contract with the company and agrees on the contract price, the entrust and the company conduct the final accounting audit according to the progress node stipulated in the contract, and the financial department of the company makes the financial accounting according to the audited amount. Upon acceptance of the project and completion of the project quality guarantee period, the entrusting party pays the project quality guarantee fund to the company.

### Sales Business

As an important source of revenue for PCHG, the sales business segment makes the company's business more diversified and plays a complementary role to its main business.

PCHG mainly engaged in the sales of concrete and seedlings. There was a high concentration of suppliers and customers, and the counterparty was mainly private enterprises and individuals, with a certain counterparty risk.

### Other Businesses

Other businesses of PCHG include road tolling, passenger transport, leasing and advertising design, 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.

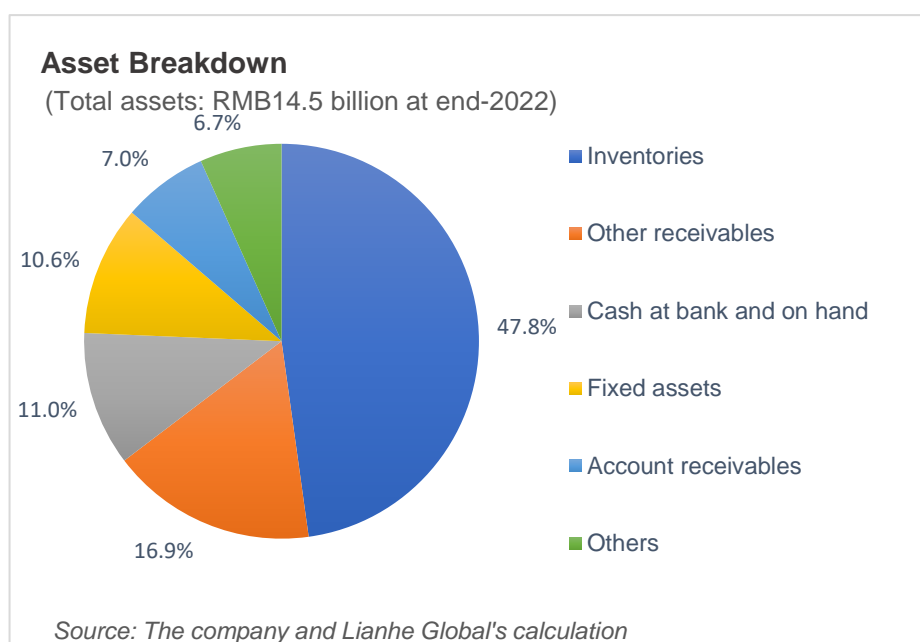
## Financial Profile

### Balance Sheet Structure and Quality

<b>Balance Sheet Structure and Quality</b>			
<b>(RMB million)</b>	<b>2020</b>	<b>2021</b>	<b>2022</b>
Total Asset	10,605	12,347	14,453
Equity	6,839	7,183	7,382
Debt	2,189	3,838	5,423
Debt / (Debt + Equity) (%)	24.3	34.8	42.35
LT Debt	407	721	2,165
LT Debt / (LT Debt + Equity) (%)	5.6	9.1	22.68

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

PCHG's total assets showed a continuous growth in the past few years, with a growth rate of 16.4% and 17.1% at end-2021 and end-2022, respectively, and reached RMB14.5 billion at end-2022. The increase of PCHG's total assets in 2022 was largely due to its inventories and other receivables. PCHG's assets mainly consisted of inventories, receivables, cash at bank and on hand and fixed assets. The scale of inventories was large that mainly included contract performance costs and costs of land to be developed, which increased in parallel with the growth of the relevant projects. Other receivables and account receivables were mainly transactions (project payments, current payments and advance payments) with local government departments and state-owned enterprises in the region, and sales payments with a Hong Kong enterprise, Hong Kong Yongxiang Development Co., LTD., which had an aging period of mostly 1-3 years, with controllable counterparty risk and low bad debt provision. Fixed assets primarily comprised of houses and buildings. Although the company's asset structure was dominated by current assets, the inventories monetization was heavily influenced by the progress of government settlements, the use of some assets was restricted and some funds were occupied by accounts receivable. Therefore, the company's overall asset liquidity was weak.



PCHG's financial leverage (total liabilities to assets) reached 35.5%, 41.8% and 48.9% at end-2020, end-2021 and end-2022, respectively, representing an upward trend due to the increase in bank borrowings and financial leasing, as well as the bank debt financing in 2022. PCHG's total adjusted debt increased by 147.7% from c. RMB2.2 billion at end-2020 to c. RMB5.4 billion at end-2022, mainly due to the increase of external financing of the company with the continuous investment in the project and business expansion. The short-term debt and long-term debt accounting for c. 60.1% and c. 39.9% of the total debt at end-2022. There was no significant change in the ownership equity structure of PCHG at end-2022, compared with that at end-2021. The capital surplus increased to c. RMB6.3 billion at end-September 2022 from c. RMB6.0 billion at end-2020. PCHG mainly relies on external financing to support its capital expenditures and debt repayment, which we expect to increase in the future given its transportation related projects under construction and to be constructed in the future.

### Debt Servicing Capability

The liquidity of PCHG was tight. At end-2022, PCHG had unrestricted cash balance and unused credit facilities of c. RMB0.1 billion and RMB2.1 billion, respectively, compared with its debt due within one year of c. RMB3.3 billion at the same time. Therefore, the company needs to roll over its short-term bank borrowings (end-2022: c. RMB2.6 billion). In addition, obtaining additional financing sources or government support are also important to the company in maintaining its liquidity.

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