

Binzhou Beihai State-owned Assets Operation and Management Co., Ltd.

Initial Issuer Report

Summary	
Issuer Rating	BBB-
Outlook	Stable
Location	China
Industry	Local Investment and Development Companies
Date	7 July 2023

Lianhe Ratings Global Limited (“Lianhe Global”) has assigned ‘BBB-’ global scale Long-term Issuer Credit Rating with Stable Outlook to Binzhou Beihai State-owned Assets Operation and Management Co., Ltd. (“BBSA” or “the company”)

Summary

The Issuer Credit Rating reflects a high possibility that the de facto local government of Binzhou Beihai Economic Development Zone (“Beihai EDZ”), the Management Committee of Beihai EDZ (“Beihai EDZ MC”) would provide very strong support to BBSA if needed, in light of its full ownership of BBSA, the strategic importance of BBSA as the most important local investment and development company responsible for infrastructure investment and development in Beihai EDZ, and the linkage between the Beihai EDZ MC and BBSA, including management appointment, supervision over BBSA’s strategic development, major investment and financing plans, strategic alignment and ongoing operational and financial support. In addition, the local government may face significant negative impact on its reputation and financing activities if BBSA encounters any operational and financial difficulties.

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

Rating Rationale

Government’s Ownership and Supervision: The local government holds 100% ownership of BBSA through Economic and Trade Development Bureau (“ETDB”) of Beihai EDZ. The local government has strong control over BBSA, including management appointment and supervision of the strategic development, major investment and financing plans. In addition, the local government has formulated a performance assessment mechanism for the company and regularly appoints auditors to review the company’s financial position.

Strategic Importance and Strategic Alignment: BBSA is the most important investment and development entity in Beihai EDZ. The company is mainly responsible for developing urban infrastructure, public facilities, industrial parks and affordable houses in Beihai EDZ. As the core platform of Beihai EDZ, BBSA’s business operation has been aligned with the local government’s development plan. The company plays an important role in promoting economic and social development in Beihai EDZ.

Ongoing Government Support: BBSA has received ongoing support from the local government, including capital and assets injection, operational subsidies, etc. The company received capital injections of RMB994 million between 2020 and 2022. The injected assets mainly included cash and sea area use, which could generate stable rental income. The local government also provides annual operational subsidies of c. RMB30 million to BBSA in the past three years to support the company’s operations in relation to providing public

Key Figures of Beihai EDZ and BBSA (RMB billion)	2021	2022
Beihai EDZ		
GDP	11.3	12.8
GDP growth rate (%)	4.2	3.9
Budgetary revenue	1.7	1.8
Government fund	0.33	0.48
Transfer payment	0.16	0.23
Budgetary expenditure	1.5	1.6
BBSA		
Asset	11.6	13.9
Equity	6.8	7.1
Revenue	0.76	0.90

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

Analysts

Roy Luo, FRM
 +852 3462 9582
roy.luo@lhratingsglobal.com

Toni Ho, CFA, FRM
 +852 3462 9578
toni.ho@lhratingsglobal.com

Applicable Criteria

China Local Investment and Development Criteria (5 December 2022)

services. We expect BBSA to receive strong support from the local government in the future in light of its strategic importance.

Economy and Fiscal Strength of Beihai EDZ: Beihai EDZ maintained a high economic growth rate of 9.2% and 7.3% in 2021 and 2022, respectively. However, its aggregate GDP was moderately small, which was RMB12.8 billion in 2022. Beihai EDZ's economic growth was mainly fueled by the secondary industries in the past few years, which accounted for 74.4% of aggregate GDP in 2022. In recent years, its economic development focused on chemical, aluminum, marine industry and high-end equipment manufacturing.

The Beihai EDZ government's aggregate fiscal revenues were mainly derived from budgetary revenue. From 2020 to 2022, the Beihai EDZ government's fiscal revenue increased to RMB1.8 billion from RMB1.2 billion, with the tax revenue accounting for 78%-90% of its budgetary revenue. In addition, Beihai EDZ's fiscal self-sufficiency rate was sufficient, with a budget surplus of 11.8% in 2022.

Beihai EDZ's government debt continued to grow. At end-2022, the Beihai EDZ government's outstanding debt was RMB4.6 billion, up from RMB3.4 billion at end-2020. This was mainly due to the significant increase in special debts to support the local project development. Nevertheless, its fiscal debt ratio, as measured by total government debt outstanding/aggregate revenue, had decreased to 181.0% at end-2022 from 211.4% at end-2020, due to the larger increase of aggregate revenue.

BBSA's Financial Matrix and Liquidity Position: BBSA's total asset grew significantly to RMB15.0 billion at end-March 2023 from RMB8.6 billion at end-2020. Over the same period, the company's total debt increased by 291% to RMB5.7 billion from RMB1.4 billion. As a result, BBSA's financial leverage, as measured by debt/capitalization, reached 44.3% at end-March 2023, up from 18.2% at end-2020.

BBSA's liquidity was moderately tight. At end-March 2023, the company had a cash balance of RMB1.1 billion, compared with its short-term debt of RMB2.2 billion. In addition, the company's financing channels are limited, mainly relying on bank borrowing and non-traditional financing. Nevertheless, we expect the company to roll over most of its short-term bank borrowings (c. RMB1.2 billion at end-March 2023). At the same time, the company had unused credit lines of RMB1.1 billion.

Rating Sensitivities

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

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

Operating Environment

Economic Condition of Beihai EDZ

Located in the northern end of Shandong Province, Beihai EDZ is a provincial development zone of Binzhou City. Beihai EDZ was established in April 2010 and was upgraded to a provincial-level economic development zone in September 2010. It is one of the four port-surrounding industrial zones within the Yellow River Delta Efficient Ecological Economic Areas. Beihai EDZ has a land area of 267 square kilometers and a sea area of 329 square kilometers. At end-2022, Beihai EDZ had a resident population of 33.5 thousand, with an urbanization rate of 60.0%.

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Beihai EDZ's GDP and Fixed Asset Investment			
(RMB billion)	2020	2021	2022
GDP	9.7	11.3	12.8
-Primary industry (%)	4.5	4.2	3.9
-Secondary industry (%)	71.6	72.6	74.4
-Tertiary industry (%)	24.0	23.2	21.7
GDP growth rate (%)	2.7	9.2	7.3
Fixed asset investment growth rate (%)	7.3	14.1	25.9
Population (thousand)	33.5	33.5	33.5

Source: Public information and Lianhe Global's calculations

Fiscal Condition of Beihai EDZ

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Beihai EDZ's Fiscal Condition			
(RMB billion)	2020	2021	2022
Budgetary revenue	1.2	1.7	1.8
Budgetary revenue growth rate (%)	-1.0	46.6	15.0
Tax revenue	1.0	1.5	1.4
Tax revenue (% of budgetary revenue)	82.5	90.2	79.0
Government fund income	0.3	0.3	0.5
Transfer payment	0.1	0.2	0.2
Aggregate revenue	1.6	2.2	2.5

Budgetary expenditure	1.4	1.5	1.6
Budget deficit ¹ (%)	-22.8	13.0	11.8

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 and Profile

Government's Full Ownership

Binzhou Beihai State-owned Assets Operation Management Co., Ltd. was established in April 2014 with an initial registered capital of RMB200 million, funded by Economic Development Bureau of Beihai EDZ. After a series of equity transfers, ETDB of Beihai EDZ held 100% shares of BBSA at end-2023. The company's registered was enlarged to RMB300 million at end-June 2023.

Strategic Importance and Government Linkage

Strategic Importance of BBSA to Beihai EDZ

BBSA is the most important investment and development entity in Beihai EDZ. The company is mainly responsible for developing urban infrastructure, public facilities, industrial parks and affordable houses in Beihai EDZ. As the core platform of Beihai EDZ, BBSA's business operation has been aligned with the local government's development plan. The company plays an important role in promoting economic and social development in Beihai EDZ.

Linkage with the Local Government

BBSA's linkage with the local government is strong as the local government holds a 100% stake in BBSA through ETDB of Beihai EDZ. The local government has strong supervision over BBSA, including management appointment and supervision of the strategic development, major investment and financing plans. In addition, the local government has formulated a performance assessment mechanism for the company and regularly appoints auditors to review the company's financial position.

Government Support

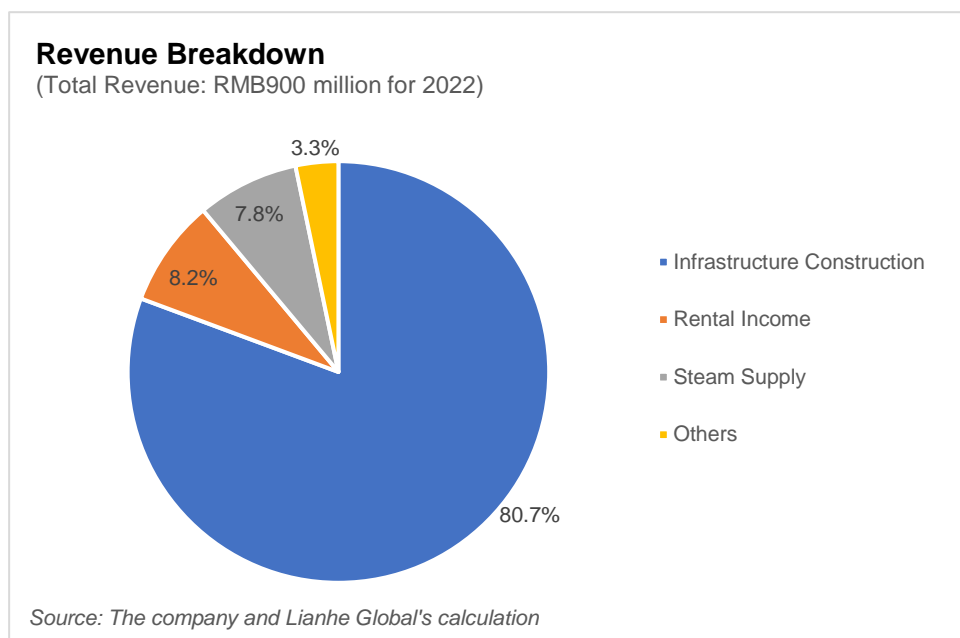
BBSA has received ongoing support from the local government, including capital and assets injection, operational subsidies, etc. The company received capital injections of RMB628 million, 161 million and 205 million in 2020, 2021 and 2022, respectively. The injected assets mainly included cash and sea area use, which could generate stable rental income. The local government also provides annual operational subsidies of c. RMB30 million to BBSA in the past three years, to support the company's operations in relation to providing public services. We expect BBSA to receive strong support from the local government in the future in light of its strategic importance.

Business Profile

The Most Important Investment and Development Entity in Beihai EDZ

BBSA is the most important investment and development entity in Beihai EDZ. The company is mainly responsible for developing urban infrastructure, public facilities, industrial parks and affordable houses in Beihai EDZ. At the same time, it also engaged in leasing sea area

use rights and underground integrated corridors, as well as supplying steam in Beihai EDZ. As the core platform of Beihai EDZ, BBSA plays an important role in promoting economic and social development within the region. The company realized total revenue of RMB685 million, RMB763 million, 900 million and RMB900 million in 2020, 2021 and 2022, respectively, demonstrating an upward trend.



Infrastructure Construction

BBSA mainly undertakes infrastructure, public facilities and affordable houses development projects in Beihai EDZ by entering into construction agreements. According to construction agreements, BBSA is usually responsible for fundraising and constructing entrusted projects. Then the company recognizes 130% of construction costs as revenue upon completion. However, some projects face a protracted cash collection period.

By end-2022, BBSA had completed most of its construction agreements. Currently, BBSA mainly adopts the self-management model to develop industrial parks and related infrastructure, such as underground integrated corridors, and water and heat supply networks. Under self-management, construction costs are supported by the company's own fund, bank borrowings and government special bonds and other financing channels; then the company uses rental and commercial operations incomes to cover the construction costs and generate returns. At end-2022, the company had three self-management projects under construction, with a total planned investment of RMB7.4 billion, which could incur high expenditure pressure of project construction in the next one to two years.

Rental Income, Steam Supply and Others

BBSA owns sea area use rights hectares for leisure and aquaculture and underground integrated corridors for leasing, which generated annual rental incomes of c. RMB42 million and RMB32 million, respectively, in 2021 and 2022, providing a stable source of income for the company.

BBSA supplies steam to industrial users in Beihai EDZ. The company purchases steam from delivers it to end-users through its self-owned steam supply network. Other businesses of the company include sales of salt and garbage disposal. These businesses mainly play the role of supplementing the revenue of the main business and making the revenue structure more diversified.

Financial Profile

Balance Sheet Structure and Quality

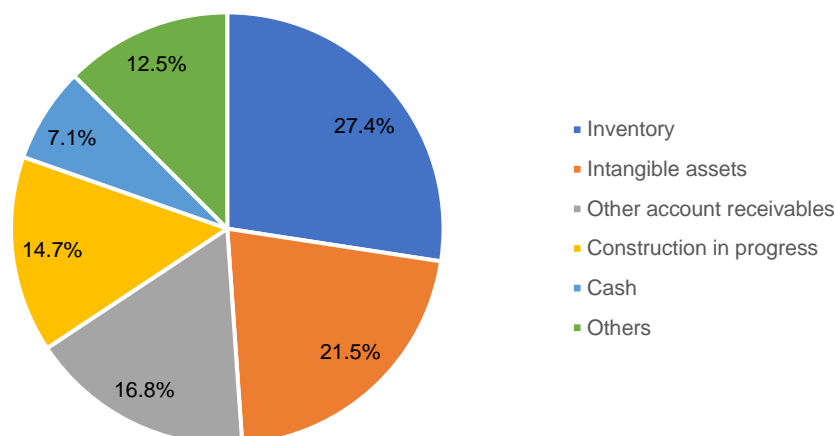
Balance Sheet Structure and Quality				
(RMB million)	2020	2021	2022	March 2023
Total Asset	8,590	11,622	13,870	15,049
Equity	6,514	6,779	7,075	7,122
Debt	1,448	3,534	4,844	5,659
Debt / (Debt + Equity) (%)	18.2	34.3	40.6	44.3
LT Debt	974	2,185	2,933	3,433
LT Debt / (LT Debt + Equity) (%)	13.0	24.4	29.3	32.5

Source: Company Information and Lianhe Global's calculations

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Asset Breakdown

(Total assets: RMB15.0 billion at end-March 2023)



Source: The company and Lianhe Global's calculation

BBSA's asset liquidity was moderately weak. The company's infrastructure construction activities accumulated sizeable inventories (mainly construction costs) and construction in progress, which amounted to RMB4.1 billion and RMB2.2 billion, representing 27.4% and 14.7% of BBSA's total asset, respectively, at end-March 2023. These assets usually take a long time to monetize due to the protracted construction and payment collection period. At the same time, BBSA had intangible assets of RMB3.2 billion, mainly land use rights and sea area use rights. The intangible assets may lack liquidity, yet they could generate stable rental income for the company. In addition, other accounts receivable, which were primarily due from other LIDCs in Beihai EDZ without a specified repayment schedule, accounted for 16.8% of BBSA's total asset.



Debt Servicing Capability

BBSA's liquidity was moderately tight. At end-March 2023, the company had a cash balance of RMB1.1 billion, compared with its short-term debt of RMB2.2 billion. In addition, the company's financing channels are limited, mainly relying on bank borrowing and non-traditional financing. Nevertheless, we expect the company to roll over most of its short-term bank borrowings (c. RMB1.2 billion at end-March 2023). At the same time, the company had unused credit lines of RMB1.1 billion.

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