

Jiangsu Anhui Cooperation Demonstration Zone Construction and Development Group Co., Ltd.

Initial Issuer Report

Summary

Issuer Rating	BBB+
Outlook	Stable
Location	China
Industry	Local Investment and Development Companies
Date	16 August 2023

Lianhe Ratings Global Limited (“Lianhe Global”) has assigned ‘BBB+’ global scale Long-term Issuer Credit Rating with Stable Outlook to Jiangsu Anhui Cooperation Demonstration Zone Construction and Development Group Co., Ltd. (“JAG” or “the company”)

Summary

The Issuer Credit Rating reflects a high possibility that the People’s Government of Liyang (“the Liyang government”) would provide strong support to JAG if needed. This mainly considers the Liyang government’s full ownership of JAG, JAG’s strategic importance as an important local investment and development company (“LIDC”) responsible for primary land development, resettlement house and infrastructure construction in Liyang, and the linkage between the Liyang government and JAG, including the appointment of senior management, strategic alignment, supervision of major investment and financing decisions and ongoing operational and financial support. In addition, the Liyang government may face significant negative impact on its reputation and financing activities if JAG encounters any operational and financial difficulties.

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

Rating Rationale

Government’s Ownership and Supervision: The Liyang government holds 100% shares of JAG through Liyang State-Owned Assets Management Center (“Liyang SAMC”) and authorizes Liyang State-Owned Assets Investment Holding Group Co., Ltd. (“LSAI”), an LIDC wholly owned by Finance Bureau of Liyang, to manage JAG. The Liyang government has strong control over the company, including the appointment of senior management and supervision of JAG’s 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: JAG is an important LIDC that is responsible for the primary land development, resettlement house and infrastructure construction in the northern part of Liyang. JAG’s business operations and strategic planning have been aligned with the local government’s economic and social development policies.

Ongoing Government Support: The local government provided ongoing support to JAG. The company received multiple cash capital injections of RMB3.3 billion, 4.4 billion and 1.2 billion in 2020, 2021 and 2022, respectively. The local government also transferred assets, mainly equity of local SOEs, valued at RMB816 million over the same period. In addition, the local government provided operational subsidies of RMB863 million in the past three years to support JAG’s activities in relation to providing public goods. We expect JAG to receive ongoing support from the local government in the coming years considering its strategic importance in Liyang.

Key Figures of Liyang and JAG (RMB billion)

Liyang	2021	2022
GDP	126.1	141.6
GDP growth rate (%)	4.5	4.1
Budgetary revenue	8.7	8.1
Government fund	27.9	28.3
Transfer payment	1.9	3.8
Budgetary expenditure	10.3	12.8
JAG	2021	2022
Asset	32.0	37.9
Equity	20.9	22.1
Revenue	1.0	1.0

Source: Public information, JAG 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 Liyang: Liyang was listed in China's top 100 counties and managed to maintain its economic growth in the past three years, with growth rates of 4.6%, 10.1% and 6.2% in 2020, 2021 and 2022. Liyang realized a GDP of RMB141.6 billion in 2022. Under the Jiangsu-Anhui Cooperation Demonstration Zone Development Plan approved by National Development and Reform Commission in 2018, Liyang has been participating in the integration development between Jiangsu province and Anhui province. Liyang is also focusing on the development of power battery, smart grid, farming and feed machinery, automotive and components industries, attracting leading manufacturer such as CATL to build production base in the region.

The aggregate fiscal revenue of the Liyang government was primarily derived from budgetary revenue and government fund income. The Liyang government's budgetary revenue decreased to RMB8.1 billion in 2022 from RMB8.7 billion in 2021, mainly due to the large-scale value-added tax refund policy to support the economy. Meanwhile, the Liyang government's budgetary expenditure increased to RMB12.8 billion in 2022 from RMB11.0 billion in 2021. As a result, the Liyang government's budget deficit widened to -57.7% in 2022 from -18.1% in 2021. Yet Liyang's government fund income, mainly generated by land sales, maintained a stable trend in the past three years and reached RMB28.3 billion in 2022, remaining the largest contributor to aggregate fiscal revenue.

The outstanding debt of the Liyang government continued to grow over the past three years. At end-2022, the Liyang government's outstanding debt reached RMB36.0 billion, representing a year-over-year growth rate of 24.2%, mainly due to the new issuance of special debt to support Liyang's project development. As a result, the government debt ratio (total government debt/aggregate revenue) increased to 89.5% in 2022 from 66.9% in 2020.

JAG's Financial and Liquidity Position: JAG's total asset grew steadily to RMB37.9 billion at end-2022 from RMB25.6 billion at end-2020, mainly supported by the multiple rounds of capital injections from the Liyang government, which enlarged its equity base to RMB22.1 billion from RMB16.3 billion during the period. The company also relied on debt financing to fund its asset expansion. As measured by total debt/capitalization, the company's financial leverage increased to 29.9% from 24.2% over the same period. Yet it stayed at a manageable level.

JAG's liquidity was tight. At end-2022, the company had cash of RMB687 million (including restricted cash of RMB203 million). At the same time, the company had debt due within one year of RMB3.3 billion. JAG has access to various financing channels, including bank borrowings and other non-traditional financings, to support its debt repayments and business operations. At end-2022, the company had unused credit lines of RMB1.4 billion, and we expect JAG to roll over most of its short-term bank borrowings (c. RMB812 million). Yet obtaining additional financing channels and timely receiving government support is still important for JAG to maintain its liquidity.

Rating Sensitivities

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

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

Operating Environment

Economic Condition of Liyang

Liyang is a county-level city directly under the jurisdiction of Jiangsu Province and managed by Changzhou on behalf of Jiangsu Province. At end-2022, Liyang has a residential population of 806 thousand, with an urbanization rate of 64.6%. Liyang is located in the southwest of Changzhou, bordering Zhejiang and Anhui provinces. Liyang has jurisdiction over nine towns and three streets, with a total land area of 1,535 square kilometers. Under the Jiangsu-Anhui Cooperation Demonstration Zone Development Plan approved by National Development and Reform Commission in 2018, Liyang has been participating in the integration development between Jiangsu province and Anhui province, which focus on the promoting transportation connectivity, industrial development and joint construction and sharing of infrastructure and public services between two provinces. Besides, it also owns one national tourism resort (Tianmu Lake), one provincial high-tech zone (Liyang High-tech Industrial Development Zone), one provincial development zone (Liyang Economic Development Zone) and one provincial tourism resort (Cao Moutain).

Liyang was listed in China's top 100 counties and managed to maintain its economic growth in the past three years, with growth rates of 4.6%, 10.1% and 6.2% in 2020, 2021 and 2022. Liyang realized a GDP of RMB141.6 billion in 2022. Liyang's economic growth was mainly fueled by the secondary and tertiary industries, which accounted for 54.2% and 41.7% of GDP in 2022, respectively. Liyang is focusing on the development of power battery, smart grid, farming and feed machinery, automotive and components industries, attracting leading manufacturer such as CATL to build production base in the region.

Liyang's GDP and Fixed Asset Investment

(RMB billion)	2020	2021	2022
GDP	108.6	126.1	141.6
-Primary industry (%)	5.0	4.5	4.1
-Secondary industry (%)	49.7	51.4	54.2
-Tertiary industry (%)	45.3	44.1	41.7
GDP growth rate (%)	4.6	10.1	6.2
Fixed asset investment growth rate (%)	5.1	8.0	10.1
Population (million)	0.8	0.8	0.8

Source: Public information and Lianhe Global's calculations

Fiscal Condition of Liyang

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Liyang's Fiscal Conditions			
(RMB billion)	2020	2021	2022
Budgetary revenue	7.4	8.7	8.1
Budgetary revenue growth rate (%)	5.0	18.3	6.0*
Tax revenue	6.3	7.6	6.8
Tax revenue (% of budgetary revenue)	85.9	87.1	83.4
Government fund income	24.0	27.9	28.3
Transfer payment	2.8	1.9	3.8
Aggregate revenue	34.2	38.6	40.2
Budgetary expenditure	11.6	10.3	12.8
Budget deficit ¹ (%)	-57.4	-18.1	-57.5

¹ Budget deficit = (1-budgetary expenditure / budgetary revenue) * 100%
 Notes: excluding the effect of value-added tax credit refund
 Source: Public information and Lianhe Global's calculations

Ownership Structure

Full Government Ownership

JAG was established in June 2016 with an initial registered capital of RMB1.5 billion and paid-in capital of RMB500 million, funded by Liyang SAMC. At end-2022, JAG's paid-in capital was enlarged to RMB1.5 billion. Liyang SAMC, as the sole controlling shareholder, held 100% of the company's equity. The Liyang government authorizes LSAI, an LIDC wholly owned by Finance Bureau of Liyang, to manage the JAG's strategic and financial planning.

Strategic Importance and Government Linkage

Strategic Importance of JAG to Liyang

JAG is an important LIDC that is responsible for the primary land development, and the construction of infrastructure and resettlement house in the northern area of Liyang. JAG's business operations and strategic planning have been aligned with the local government's economic and social development policies.

Strong Linkage with the Local Government

The Liyang government holds 100% shares of JAG through Liyang SAMC. The Liyang government has strong control over the company through LSAI, 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

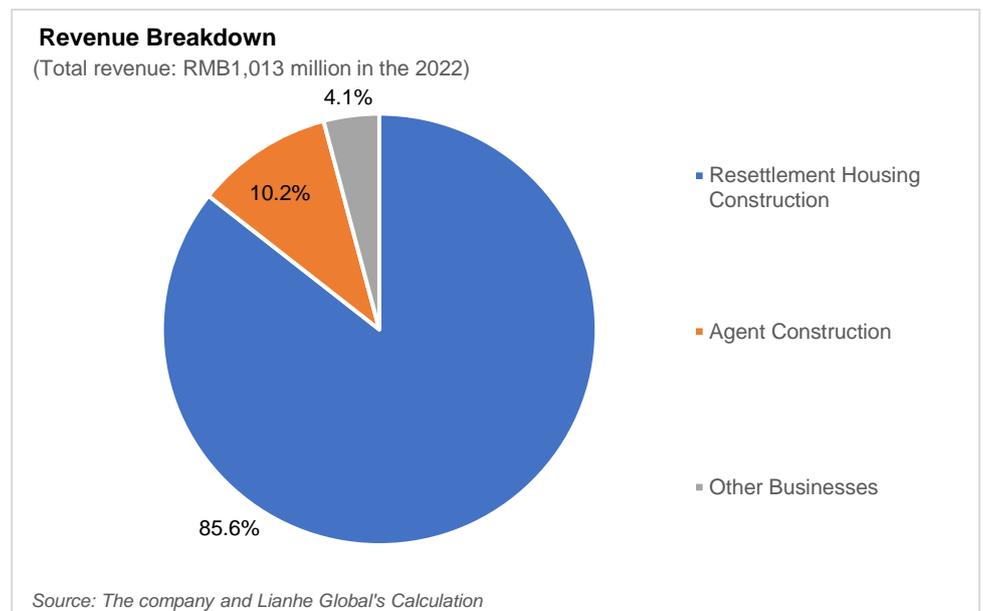
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and 2022, respectively. The local government also transferred assets, mainly equity of local SOEs, valued at RMB816 million in total over the same period. In addition, the local government provided operational subsidies of RMB863 million in the past three years to support JAG's activities in relation to providing public goods. We expect JAG to receive ongoing support from the local government in the coming years considering its strategic importance in Liyang.

Business Profile

An Important Development Entity in Liyang

As a major LIDC in Liyang, JAG is designated by the local government to undertake primary land development projects and the construction of resettlement houses, infrastructure and public facilities in the city's northern area. The primary sources of operating revenue for the company are resettlement housing construction, entrusted construction and land development, while it also engaged in parking lot management, agricultural products sales and leasing, etc. The company recorded increasing revenue of RMB887 million, 1,009 million and 1,013 million in 2020, 2021 and 2022, respectively.



Primary Land Development

As the sole entity responsible for primary land development in the northern area of Liyang, the JAG undertakes land acquisition, relocation and consolidation works within the region. The company adopts a cost-plus model, under which the company conducts primary land development following the government's land development plan. It recognizes revenue at the cost incurred plus a certain profit margin (usually 5%) upon completion, acceptance and transfer of developed lands. The performance of the primary land development sector is intrinsically tied to the land policies and urban planning strategies set forth by local governments. This has been evident in the fluctuation in the segment's revenue, which notably rose to RMB234 million in 2021, despite recording no income in 2020 and 2022.

Although the JAG has stopped entering new primary land development projects since 2020, JAG still had nine primary land development projects under construction at end-2022, with

a total planned investment of RMB30.7 billion, of which RMB18.7 billion was scheduled to be invested in the next five to ten years. The strong project pipeline could support the segment's development, yet it also brings high capital expenditure pressure on JAG. In addition, JAG may need to acquire lands that are completed but not yet available for public auction. This could further extend the project cycle and increase the company's cash demand.

Resettlement Housing Development and Agent Construction

The construction of resettlement housing has been JAG's largest revenue source in the past three years. The company acquires the land, on which it then develops resettlement houses through public bidding and auction. After completing the projects, JAG transfers and settles with the local government following the signed repurchase agreements. Generally, the local government will pay within one year. The segment has a relatively high cash collection efficiency compared to primary land development, yet its profit margin remained at a moderately low level of 1%-2% between 2020 and 2022.

In addition, JAG is designated by the Liyang government to undertake the infrastructure construction in the city's northern area and enjoys a strong franchise advantage within the region. The project scope mainly included urban infrastructure, public facilities and landscaping. The company signs agreements with the government or government-related agencies, under which the company is responsible for project investment and financing as well as construction management, and the entrusted party will pay upon project completion at the price of construction costs plus a profit of 3%-5%. However, the actual payment schedule is subject to the local government's fiscal conditions.

At end-2022, JAG had four resettlement housing and ten agent construction projects under construction, which acquired capital expenditure of c. RMB4.6 billion in the next two to three years.

Other Businesses

JAG is also involved in parking lot management, agricultural products sales and leasing, with each segment accounting 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 making the revenue structure more diversified.

Financial Profile

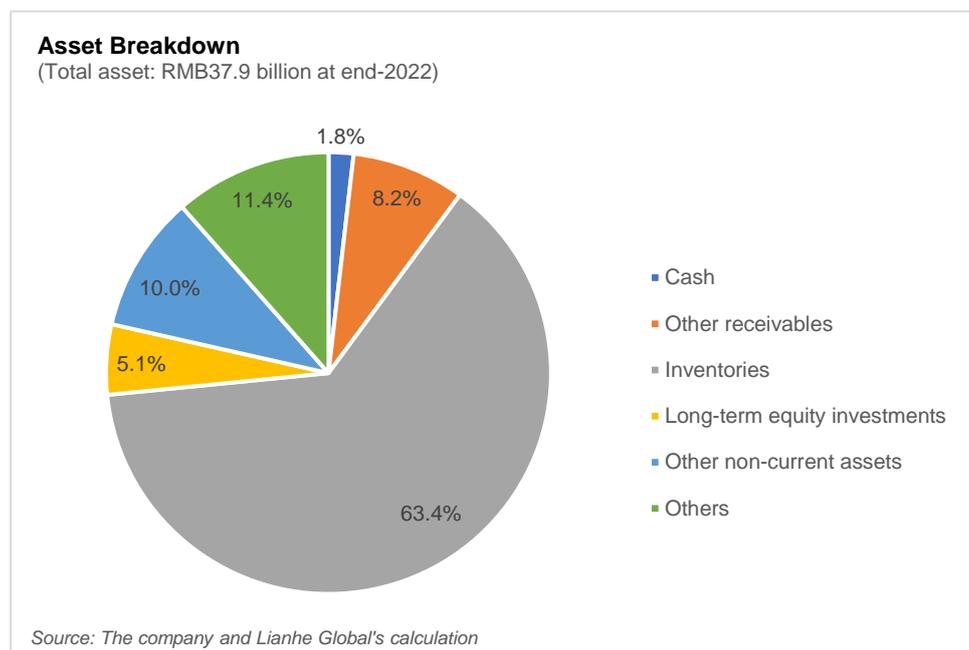
Balance Sheet Structure and Quality

Balance Sheet Structure and Quality			
(RMB million)	2020	2021	2022
Total Asset	25,597	32,015	37,946
Equity	16,324	20,937	22,133
Debt	5,218	8,003	9,461
Debt / (Debt + Equity) (%)	24.2	27.7	29.9
LT Debts	3,109	5,514	6,170
LT Debt / (LT Debt + Equity) (%)	16.0	20.8	21.8

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

JAG's total asset grew steadily to RMB37.9 billion at end-2022 from RMB25.6 billion at end-2020, mainly supported by the multiple rounds of capital injections from the Liyang

government, which enlarged its equity base to RMB22.1 billion from RMB16.3 billion during the period. The company also relied on debt financing to fund its asset expansion. As measured by total debt/capitalization, the company's financial leverage increased to 29.9% from 24.2% over the same period. Yet it stayed at a manageable level.



JAG's asset quality was moderately weak. As the company actively participated in project development in Liyang, it accumulated sizeable inventories (mainly construction costs), which increased by 58.3% to RMB24 billion at end-2022 from RMB15.2 billion at end-2020. Inventories represent the largest part of JAG's assets and usually take a long time to monetize due to protracted construction, recognition and cash collection period.

In addition, JAG had other non-current assets amounting to RMB3.8 billion, which mainly comprised lands land-transferring fees and related taxes and expenses paid to the local government. However, JAG had not obtained the land titles after paying such fees yet. The company plans to develop resettlement houses, residential and commercial properties on these lands.

At end-2022, JAG had other receivables of RMB3.1 billion, mainly due from Liyang's government agencies, SOEs and LIDCs. Yet other receivables usually have no specific collection schedule. At the same time, JAG also had long-term equity investments in other LIDCs and SOEs in Liyang, amounting to RMB1.9 billion. We believe these assets also lack liquidity.

Debt Servicing Capability

JAG's liquidity was tight. At end-2022, the company had cash of RMB687 million (including restricted cash of RMB203 million). At the same time, the company had debt due within one year of RMB3.3 billion. JAG has access to various financing channels, including bank borrowings and other non-traditional financings, to support its debt repayments and business operations. At end-2022, the company had unused credit lines of RMB1.4 billion, and we expect JAG to roll over most of its short-term bank borrowings (c. RMB812 million). Yet obtaining additional financing channels and timely receiving government support is still important for JAG to maintain its liquidity.

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