

Fuyang Yingquan Industrial Investment Development Co., Ltd.

Initial Issuer Report

Summary

Issuer Rating	BBB-
Outlook	Stable
Location	China
Industry	Local Investment and Development Companies
Date	22 November 2023

Lianhe Ratings Global Limited (“Lianhe Global”) has assigned ‘BBB-’ global scale Long-term Issuer Credit Rating with Stable Outlook to Fuyang Yingquan Industrial Investment Development Co., Ltd. (“FYIID” or “the company”)

Summary

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

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

Rating Rationale

Yingquan Government’s Ownership and Supervision: The Yingquan government holds the full ownership of FYIID through the Fuyang City Yingquan District State-owned Assets Supervision and Administration Commission (“Yingquan SASAC”). The Yingquan government is the actual controller of the company. It 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 Yingquan government has assessment mechanism over the company and appoints auditors to supervise the operating performance and financial position on a periodic basis.

Strategic Importance to Yingquan and Strategic Alignment: FYIID, as the key LIDC in Yingquan, is primarily responsible for the construction of industrial-related infrastructure and industrial development within Yingquan, especially in the Anhui Fuyang Yingquan Economic Development Zone (“Yingquan EDZ”). With a focus on industrial development in the area, the company engages in activities such as industrial park construction, industrial investments, and related road and utility network construction within the region. Additionally, the company is involved in the construction of industrial buildings, talent apartments, and other supporting facilities in the industrial parks it constructed, with strong regional advantages. The company’s business operation and development have been aligned with the government’s development plans.

Ongoing Government Support: FYIID received operational and financial support from the government. FYIID received a total subsidy of RMB488.8 million from 2020 to 2022. The Yingquan government continued to inject capital and other assets into FYIID to expand its asset size. Besides, the Anhui Yingquan Economic Development Zone Management Committee (“EDZ MC”) will repurchase some infrastructure projects and provide policy supports to FYIID to ensure its business operation. Given that it is the major entity for

Key Figures of Yingquan and FYIID

(RMB billion)	2021	2022
Yingquan		
GDP	25.4	26.9
GDP growth rate (%)	9.4	5.1
Budgetary revenue	1.1	1.0
Government fund	0.0	0.0
Transfer payment	5.4	2.6
Budgetary expenditure	3.6	3.2
FYIID		
Assets	6.2	10.6
Equity	4.7	6.8
Revenue	0.5	0.7

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

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Applicable Criteria

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

infrastructure construction and industrial park construction in Yingquan EDZ, FYIID has an advantage in acquiring land resources and major projects. We believe FYIID is likely going to receive government support to support its daily business operation.

FYIID's Financial Matrix and Liquidity Position: FYIID's total assets showed a continuous growth trend in the past years and reached RMB10.6 billion at end-2022, mainly due to the increase of inventories, which have steadily increased in tandem with the company's infrastructure construction projects. The current assets of FYIID accounted for 68.6% of total assets at end-2022, but the overall asset liquidity was moderately weak due to large proportion of inventories and receivables.

FYIID's financial leverage (total liabilities to total assets) was 36.5% and its adjusted debt increased to RMB3.2 billion at end-2022 from RMB1.4 billion at end-2021. The liquidity of FYIID was sufficient. FYIID had a cash balance and unused credit facilities of RMB671.9 million and RMB1.2 billion at end-2022, respectively, compared with its debt due within one year of RMB749.5 million. Besides, FYIID has access to various financing channels, including bank loans and non-traditional financing, to support its debt repayment and business operations.

Economy and Fiscal Condition of Yingquan: Yingquan is a district of Fuyang City ("Fuyang"), Anhui Province ("Anhui") and lies in the center of Fuyang with a total land area of 641 square kilometers. Yingquan's GDP growth rate fluctuated in the past three years, which was 3.8%, 9.4% and 5.1% in 2020, 2021 and 2022, respectively. Its GDP reached RMB39.1 billion in 2022, which was ranked 7th out of all jurisdictions among all counties and districts under Fuyang's jurisdictions.

The aggregate fiscal revenue of the Yingquan government was mainly derived from the budgetary revenue and transfer payment from the higher government. The Yingquan government's budgetary revenue was volatile in the past three years, decreasing from RMB1.1 billion in 2020 to RMB1.0 billion in 2022. The financial sufficiency of Yingquan government was improving but still weak, and the budget deficit narrowed to 214.5% in 2022 from 268.5% in 2020. The fiscal debt ratio (total government debt outstanding/aggregate revenue) of the Yingquan government surged to 264.4% in 2022, more than doubled compared with that in 2020.

Rating Sensitivities

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

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

Operating Environment

Economic Condition of Yingquan

Yingquan is a district that lies in the center of Fuyang. Yingquan has jurisdiction over 4 towns, 2 streets, 1 pilot area and 1 industrial park, with a total area of 641 square kilometers. Owing to Covid's disruption, Yingquan's GDP growth rate fluctuated in the past three years, which was 3.8%, 9.4% and 5.1% in 2020, 2021 and 2022, respectively. The GDP amount of

Yingquan reached RMB39.1 billion in 2022, which was ranked 7th among all counties and districts under Fuyang's jurisdictions. The economic growth of Yingquan was mainly fueled by the secondary and tertiary industries in the past few years, which accounted for 31.3% and 56.9% in 2022, respectively. The fixed asset investment of Yingquan maintained a rapid growth in 2020-2022, and the amount of fixed asset investment increased to RMB28.2 billion in 2022 from RMB20.2 billion in 2020.

Yingquan EDZ was established in 2014. It is a Provincial Economic and Technological Development Zone. Currently, Yingquan EDZ has three leading industries, including light industry and textile, machinery and electronics, plate furniture. The GDP of the Yingquan EDZ has demonstrated consistent growth, propelled by robust fixed asset investments. Moreover, its contribution to the overall GDP of Yingquan has remained remarkable.

Yingquan's GDP and Fixed Asset Investment			
(RMB billion)	2020	2021	2022
GDP	23.3	25.4	26.9
-Primary industry (%)	12.4	12.0	11.8
-Secondary industry (%)	31.3	31.2	31.3
-Tertiary industry (%)	56.3	56.8	56.9
GDP growth rate (%)	3.8	9.4	5.1
Fixed asset investment	20.2	24.0	28.2
Fixed asset investment growth rate (%)	11.4	18.6	17.4
Population (million)	0.6	0.6	0.6

Source: Public information and Lianhe Global's calculations

Fiscal Condition of Yingquan

The aggregate fiscal revenue of the Yingquan government was mainly derived from budgetary revenue and transfer payment from the higher governments. The Yingquan government's budgetary revenue was volatile in the past three years, decreasing from RMB1.1 billion in 2020 to RMB1.0 billion in 2022. Meanwhile, the proportion of tax revenue over budgetary revenue dropped from 67.5% in 2020 to 59.8% in 2022. The financial sufficiency of Yingquan government was improving but still weak, and the budget deficit narrowed to 214.5% in 2022 from 268.5% in 2020. Yingquan depended crucially on transfer payment from the higher governments, with the proportion of received transfer payment in the aggregate fiscal revenue ranging from 72.3% to 82.2% in the past three years.

The outstanding amount of Yingquan government's debts showed a rapid growth in 2020-2022, increasing from RMB7.6 billion at end-2020 to RMB9.7 billion at end-2022, mainly due to the increase in special debt. The fiscal debt ratio (total government debt outstanding/aggregate revenue) of the Yingquan government surged to 264.4% in 2022, more than doubled compared with that in 2020.

Yingquan's Fiscal Condition			
(RMB billion)	2020	2021	2022
Budgetary revenue	1.1	1.1	1.0
Budgetary revenue growth rate (%)	-9.5	1.4	-12.0
Tax revenue	0.8	0.7	0.6
Tax revenue (% of budgetary revenue)	67.5	65.0	59.8
Government fund income	0.0	0.0	0.0
Transfer payment	4.8	5.4	2.6
Aggregate revenue	6.0	6.5	3.7
Budgetary expenditure	4.1	3.6	3.2
Budget balance ¹ (%)	-268.5	-218.6	-214.5

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

Source: Public information and Lianhe Global's calculations

Ownership Structure

Government's Ownership

FYIID was established in March 2017 with an initial registered capital of RMB200.0 million, funded by Yingquan SASAC. As of end-2022, the company was solely owned by Yingquan SASAC with a registered capital of RMB200 million and a paid-in capital of RMB80 million.

Strategic Importance and Government Linkage

Strategic Importance of FYIID to Yingquan

FYIID, as the key LIDC in Yingquan, is primarily responsible for the construction of industrial-related infrastructure and industrial development within Yingquan, especially in Yingquan EDZ. With a focus on industrial development in the area, the company engages in activities such as industrial park construction, industrial investments, and related road and utility network construction within the region. Additionally, the company is involved in the construction of industrial buildings, talent apartments, and other supporting facilities in the industrial parks it constructed, with strong regional advantages. The company's business operation and development have been aligned with the government's development plans.

Strong Linkage with the Local Government

FYIID's linkage with the local government is strong as the Yingquan government holds the full ownership of FYIID through Yingquan SASAC. The Yingquan 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 Yingquan government has assessment mechanism over the company and it appoints auditors to supervise the operating performance and financial position on a periodic basis.

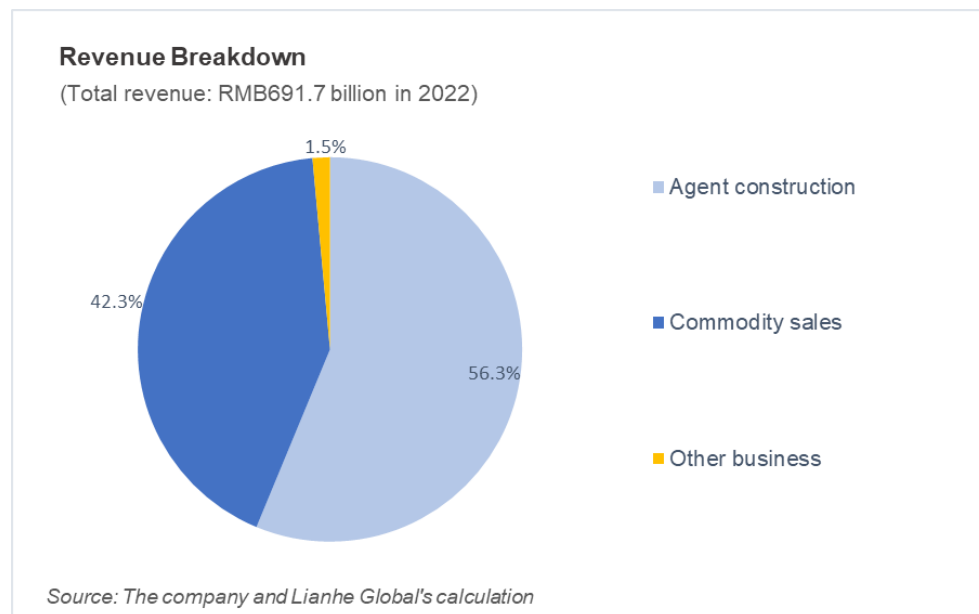
Government Support

FYIID continued to receive financial subsidies, mainly including operating subsidies (such as infrastructure construction subsidies and tax breaks), from the local government to maintain its business operation. FYIID received subsidies of RMB488.8 million from 2020 to 2022. The Yingquan government injected cash of RMB40million and RMB20 million to the company in 2020 and 2021, respectively. Besides, the Yingquan government injected some industrial properties, real estate assets, land assets to FYIID to expand its asset size. The EDZ MC will repurchase some infrastructure projects and provide policy supports to FYIID to ensure its business operation. Given that it is the major entity for infrastructure construction and industrial park construction in Yingquan EDZ, FYIID has an advantage in acquiring land resources and major projects. We believe FYIID is likely going to receive government support to support its daily business operation.

Business Profile

The Key Entity Responsible for Infrastructure Construction and Industrial Development within Yingquan EDZ

FYIID is an important LIDC that operates in infrastructure construction and industrial development within the Yingquan EDZ, and enjoys a strong regional advantage. In addition, the company also engages in businesses like industrial investment, commodity sales, financial leasing and property management to diversify its business structure. The total revenue of FYIID reached RMB333.5 million, RMB471.6 million and RMB691.7 million in 2020, 2021 and 2022, respectively. The overall gross profit margin of the company was stable, recorded at 14.2%, 12.6% and 12.3% in the corresponding period.



Agent Construction

The company is responsible for the infrastructure construction business in Yingquan EDZ and enjoys a strong franchise within the region, adopting the agent construction mode. The construction mainly focuses on the road and utility network, industrial buildings, talent apartments, and other supporting commercial facilities in the region. The company signs Agent Construction Contracts with the Yingquan EDZ MC and operates infrastructure construction and management work according to the requirements. The entrusting party will repurchase the project with an added margin (around 10%) on top of the total construction cost upon completion and handover. As the most important business of the company, the projects construction business achieved a revenue of RMB329.3 million, RMB398.2 million, and RMB389.1 million in 2020, 2021 and 2022, respectively. The gross profit margin of this segment showed a stable trend at around 15% in the past two years. Considering the large scale of the projects under construction or to be constructed, FYIID may face a high pressure on its capital expenditure.

Commodity Sales

FYIID's commodity sales business is large in scale. The products sold are mainly home appliances and ancillary products, magnetic strips and new energy raw material products. FYIID has established long-term cooperative relationships with upstream producers, which offers the company the opportunity to purchase at lower prices. The revenue generated from commodity sales segments reached RMB2.3 million, RMB69.3 million and RMB292.5 million in 2020, 2021 and 2022, respectively, accounting for a relatively high and gradually increasing share of the total revenue. With the stabilization of relationships with both

upstream and downstream customers, the gross profit margin of this segment increased from 1.1% in 2021 to 8.6% in 2022.

Other businesses

HNTIG's business is diversified. It engages in industrial investments, including equity investments, bond investments, and fund investments. Additionally, it engages in supply chain financing, financial leasing, and property management services etc. We believe that those businesses have a relatively small impact on the company's overall credit profile, as they only contributed a small proportion to the company's total revenue.

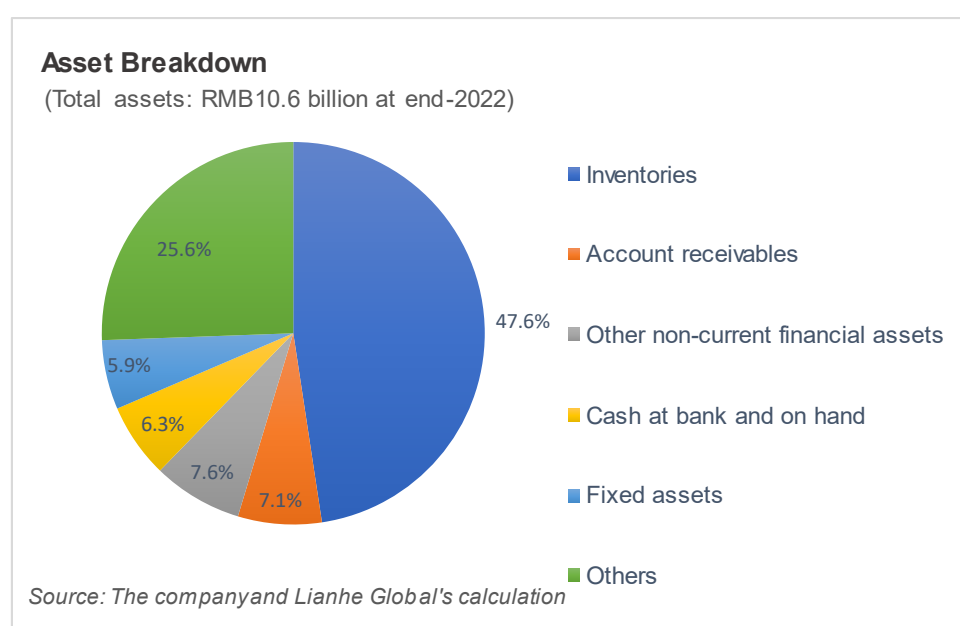
Financial Profile

Balance Sheet Structure and Quality

Balance Sheet Structure and Quality			
(RMB million)	2020	2021	2022
Total Asset	5,509	6,181	10,649
Equity	4,370	4,679	6,763
Debt	570	1,353	3,154
Debt / (Debt + Equity) (%)	11.5	22.4	31.8
LT Debt	159	702	2,405
LT Debt / (LT Debt + Equity) (%)	3.5	13.0	26.2

Source: Company information and Lianhe Global's calculations

FYIID's total assets showed a continuous growth in the past few years, with a growth rate of 12.2% and 72.3% in 2021 and 2022, respectively, and reached RMB10.6 billion at end-March 2023. The increase of FYIID's total assets was largely due to the inventories, which have steadily increased in tandem with the company's infrastructure construction projects. FYIID's assets mainly consisted of inventories, account receivables, other non-current financial assets, cash at bank and on hand and fixed assets.



FYIID's asset liquidity was moderately weak, primarily attributed to a substantial portion of inventories and account receivables, collectively accounting for 54.7% of the company's total assets as of end-2022. Most of these assets were related to the company's infrastructure construction business. The company's inventories mainly comprised land transferred from the Yingquan government and construction costs, which usually need a relatively long time to monetize due to the long construction and cash collection period. In addition, FYIID had account receivables of RMB752.3 million at end-2022, with relatively high concentration of indebted parties and high bad debt provision (RMB810.8 million at end-2022). The large provision for bad debts was due to the consolidation of the listed company, JiaWei Renewable Energy Co., Ltd. ("JiaWei"), by the company in 2022, which had a significant amount of bad debts in its accounts receivable. Excluding JiaWei, the company's bad debts provision was relatively low as most of the company's counterparties were government entities or other state-owned enterprises, posing minimal cash collection risks.

FYIID's financial leverage (total liabilities to assets) reached 20.7%, 24.3% and 36.5% at end-2020, end-2021 and end-2022, respectively, representing an increasing trend. The potential increase is contingent upon the requirements of ongoing project construction, with a limit set to comply with government oversight. FYIID's total adjusted debt increased from RMB570 million at end-2020 to RMB3.2 billion at end-2022 due to the increase of bank borrowings, with short-term debt accounting for 23.8% of the total debt. There was no significant change in the ownership equity structure of FYIID at end-2022, compared with that at end-2020. FYIID mainly relies on external financing to support its capital expenditures, 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 FYIID was sufficient. FYIID had a cash balance and unused credit facilities of RMB671.9 million and RMB1.2 billion at end-2022, respectively, compared with its debt due within one year of RMB749.5 million. Besides, FYIID has access to various financing channels, including bank loans and non-traditional financing, to support its debt repayment and business operations.

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