

# Weihai Hongtai Investment Holding Group Co., Ltd.

## Initial Issuer Report

### Summary

Issuer Rating	BBB+
Outlook	Stable
Location	China
Industry	Local Investment and Development Companies
Date	3 January 2024

Lianhe Ratings Global Limited (“Lianhe Global”) has assigned ‘BBB+’ global scale Long-term Issuer Credit Rating with Stable Outlook to Weihai Hongtai Investment Holding Group Co., Ltd. (“WHIH” or “the company”)

### Summary

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

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

### Rating Rationale

**Weihai Government’s Ownership and Supervision:** The Weihai government holds 100% ownership of WHIH through the Weihai State-owned Asset Supervision and Administration Committee (“Weihai SASAC”). The local government has the final decision-making authority and supervision over the company, including management appointment, decision on its strategic development and investment plan and supervision of its major funding decisions. The local government also coordinates WHIH’s financings and debt repayments. In addition, the local government has assessment mechanism over the company and appoints auditors to supervise the operating performance and financials on a periodic basis.

**Strategic Importance and Alignment:** As the local government transferred an array LIDCs’ equity and other assets to WHIH, the company has become one of the largest LIDC in terms of asset size in Weihai. It focuses on the construction of infrastructure, industrial parks and other municipal facilities in Weihai’s Wendeng District. The company’s business operation and strategic planning have been aligned with the government’s development plans, playing a significant role in promoting the economic and social development of the region.

**Ongoing Government Support:** WHIH receive ongoing government support in forms of capital/asset injections and financial subsidies to support its business operations. The company received financial subsidies amounting to RMB4.6 billion between 2020 and the first nine months of 2023 from the local government. Over the same period, the local government also injected fiscal funds, pipe network and use right of sea area totaling RMB6.1 billion. We believe that the local government support will remain intact given the company’s strategic importance in Weihai.

**Economy and Fiscal Condition of Weihai:** Weihai is a prefecture-level city under the jurisdiction of Shandong Province and located at the eastern end of Shandong Peninsula, bordering the Yellow Sea on three sides. As a regional hub city in Shandong Peninsula, Weihai boasts abundant marine resources and tourism attractions.

### Key Figures of Weihai and WHIH

#### (RMB billion)

Weihai	2021	2022
GDP	336.0	340.8
GDP growth rate (%)	7.4	1.5
Budgetary revenue	26.7	22.5
Government fund	40.3	31.0
Transfer payment	10.2	12.0
Budgetary expenditure	34.4	40.1
WHIH	2022	2023.9
Asset	65.4	65.5
Equity	43.6	43.2
Revenue	4.4	3.0

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

### Analysts

Karis Fan, CESGA  
 (852) 3462 9579  
[karis.fan@lhratingsglobal.com](mailto:karis.fan@lhratingsglobal.com)

Roy Luo, FRM, CESGA  
 (852) 3462 9582  
[roy.luo@lhratingsglobal.com](mailto:roy.luo@lhratingsglobal.com)

### Applicable Criteria

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

Weihai's GDP per capita was relatively high, recording RMB116,900 in 2022, higher than Shandong's RMB86,000. However, its GDP growth rate fluctuated in the past three years, owing to Covid's disruption, which was 3.0%, 7.5% and 1.5% in 2020, 2021 and 2022, respectively. The fixed asset investment fell by 18.9% in 2022, owing to significant drop of property investment.

The Weihai government's aggregate fiscal revenues are mainly derived from budgetary revenue and government fund income. The Weihai government's budgetary revenue decreased to RMB22.5 billion in 2022 from RMB26.7 billion in 2021, mainly due to the large-scale value-added tax credit refund policy to support the economy. On the other hand, the government fund income, mainly generated by land sales, slumped by 23.1% year-over-year to RMB31.0 billion in 2022, owing to the weak property market. The Weihai government's fiscal self-sufficiency rate was relatively low, and it recorded a budget deficit of 78.2% in 2022.

The outstanding debt of the Weihai government continued to grow in the past three years, recording at RMB89.5 billion at end-2022. Its fiscal debt ratio, as measured by total government debt outstanding/aggregate revenue, had increased to 136.7% at end-2022 from 91.9% at end-2020, mainly due to the new issuance of in special debt to support infrastructure, industrial parks and other public projects.

**WHIH's Financial and Liquidity Position:** WHIH's total asset grew steadily to RMB65.5 billion end-September 2023 from RMB51.3 billion at end-2020. The company mainly relied on capital and asset injections from the local government to fund its asset expansion. Therefore, the company's financial leverage, as measured by debt/capitalization was largely stable and manageable, recording at 27% at end-September 2023.

WHIH's asset quality was moderately weak, as it had a large size of inventories (mainly lands to be developed and construction costs for its project construction activities), which amounted to RMB45.3 billion at end-September 2023, representing 69.2% of total asset. The company has no specific development plan for its inventory lands, while the cash collection schedule for construction costs is subject to the local government's fiscal condition.

The liquidity of WHIH was tight. At end-September 2023, the company had cash balance of RMB1.8 billion (including restricted cash of RMB1.6 billion), compared with its debt due within one year of RMB4.6 billion. At the same time, the company only had unused bank facilities of RMB778 million. We expect the company to roll over most of its short-term bank borrowings (end-September 2023: c. RMB2.0 billion). Yet obtaining additional financing channels and timely government support are important for WHIH to maintain its liquidity.

## Rating Sensitivities

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

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

## Operating Environment

### Economic Condition of Weihai

Weihai is a prefecture-level city under the jurisdiction of Shandong Province and located at the eastern end of Shandong Peninsula, bordering the Yellow Sea on three sides. As a regional hub city in Shandong Peninsula, Weihai boasts abundant marine resources and tourism attractions. Weihai has jurisdiction over 2 districts and 2 county-level cities, with a total area of 5,800 square kilometers. At end-2022, Weihai had a resident population of 2.92 million, with an urbanization rate of 71.8%.

Weihai's GDP per capita was relatively high, recording RMB116,900 in 2022, higher than Shandong's RMB86,000. However, its GDP growth rate fluctuated in the past three years, owing to Covid's disruption, which was 3.0%, 7.5% and 1.5% in 2020, 2021 and 2022, respectively. The fixed asset investment fell by 18.9% in 2022, owing to significant drop of property investment.

<b>Weihai's GDP and Fixed Asset Investment</b>			
<b>(RMB billion)</b>	<b>2020</b>	<b>2021</b>	<b>2022</b>
GDP	298.4	336.0	340.8
-Primary industry (%)	10.1	10.4	10.4
-Secondary industry (%)	38.4	38.8	38.5
-Tertiary industry (%)	51.5	50.8	51.1
GDP growth rate (%)	3.0	7.5	1.5
Fixed asset investment growth rate (%)	2.9	6.0	-18.9
Population (million)	2.91	2.91	2.92

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

### Fiscal Condition of Weihai

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<b>Weihai's Fiscal Condition</b>			
<b>(RMB billion)</b>	<b>2020</b>	<b>2021</b>	<b>2022</b>
Budgetary revenue	25.2	26.7	22.5
Budgetary revenue growth rate (%)	1.0	5.7	-8.9*
Tax revenue	19.0	19.9	15.9
Tax revenue (% of budgetary revenue)	75.2	74.5	70.4
Government fund income	43.8	40.3	31.0
Transfer payment	10.5	10.2	12.0
<b>Aggregate revenue</b>	<b>79.9</b>	<b>77.2</b>	<b>65.5</b>

Budgetary expenditure	35.0	34.4	40.1
Budget balance <sup>1</sup> (%)	-38.8	-28.7	-78.2

<sup>1</sup> Budget balance = (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

WHIH was established in March 2015 with an initial registered capital of RMB2.0 million. By end-June 2021, WHI's registered capital was enlarged to RMB2 billion, the Weihai Wendeng District State-owned Assets Service Center owned 100% shares of the company. In December 2021, Weihai SASAC became the sole shareholder and actual controller of the company.

## Strategic Importance and Government Linkage

### Strategic Importance of WHIH to Weihai

As the local government transferred an array of LIDCs' equity and other assets to WHIH, the company has become one of the largest LIDCs in terms of asset size in Weihai. It focuses on the construction of infrastructure, industrial parks and other municipal facilities in Weihai's Wendeng District. The company's business operation and strategic planning have been aligned with the government's development plans, playing a significant role in promoting the economic and social development of the region.

### Strong Linkage with the Local Government

WHIH's linkage with the local government is strong as the Weihai government holds 100% ownership of WHIH through the Weihai SASAC. The local government has the final decision-making authority and supervision over the company, including management appointment, decision on its strategic development and investment plan and supervision of its major funding decisions. The local government also coordinates WHIH's financings and debt repayments. In addition, the local government has an assessment mechanism over the company and appoints auditors to supervise the operating performance and financials on a periodic basis.

### Ongoing Government Support

WHIH receives ongoing government support in forms of capital/asset injections and financial subsidies to support its business operations. The company received financial subsidies amounting to RMB4.6 billion between 2020 and the first nine months of 2023 from the local government. Over the same period, the local government also injected fiscal funds, pipe network and use right of sea area totaling RMB6.1 billion. We believe that the local government support will remain intact given the company's strategic importance in Weihai.

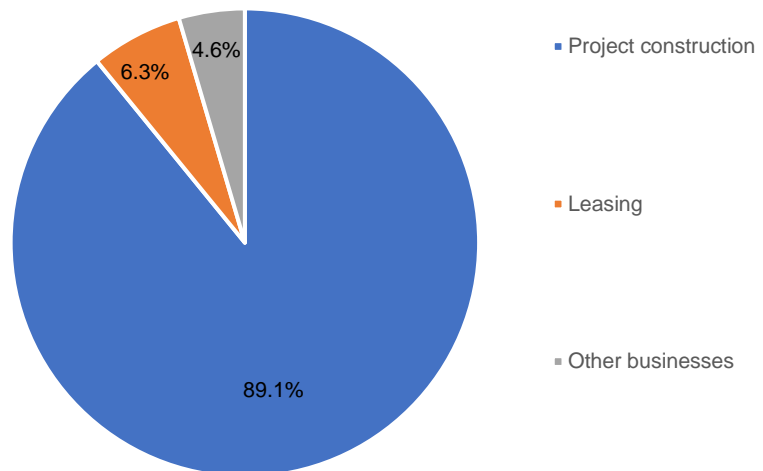
## Business Profile

### The Important Entity Responsible for Infrastructure Construction in Weihai's Wendeng District

WHIH, as an important LIDC in Weihai, focus on the construction of infrastructure, industrial parks and other municipal facilities in Wendeng District. The primary source of operating revenue for WHIH is project construction, while it also engaged in leasing, thermoelectricity, security service, etc. The company's total revenue reached RMB4.3 billion, RMB4.3 billion, RMB4.4 billion and RMB3.0 billion in 2020, 2021, 2022 and the first nine months of 2023, respectively. Its gross profit margin fluctuated between 6% and 11% over the same period. Overall, the company's business structure is relatively concentrated and it has a regional advantage over its main business.

#### Revenue Breakdown

(Total revenue: RMB3.0 billion in the first nine months of 2023)



Source: The company and Lianhe Global's Calculations

### Project Construction

WHIH is designated by the local government to undertake infrastructure and other construction projects in Wendeng District. The company adopts both agent construction and self-operated models. Under the agent construction model, the company signs the agent construction agreements with the local government and is responsible for fundraising and construction of entrusted projects. The company settles construction costs plus a percentage of management fees annually with the Wendeng government according to the project's progress. Under the self-operated model, the company constructs the projects with internal and external funds and operates them for rental income upon completion.

Currently, projects under construction and to be constructed still require a large scale of investment (approximately RMB8.4 billion in the coming years), incurring a high capital expenditure pressure on WHIH.

## Leasing and Others

As a supplementary source of revenue for the company, leasing business mainly involves the leasing of pipeline network and properties. The company also operates other businesses including thermoelectricity, security service, etc. They mainly play a supplementary role and have little impact on the company's financial position and creditworthiness.

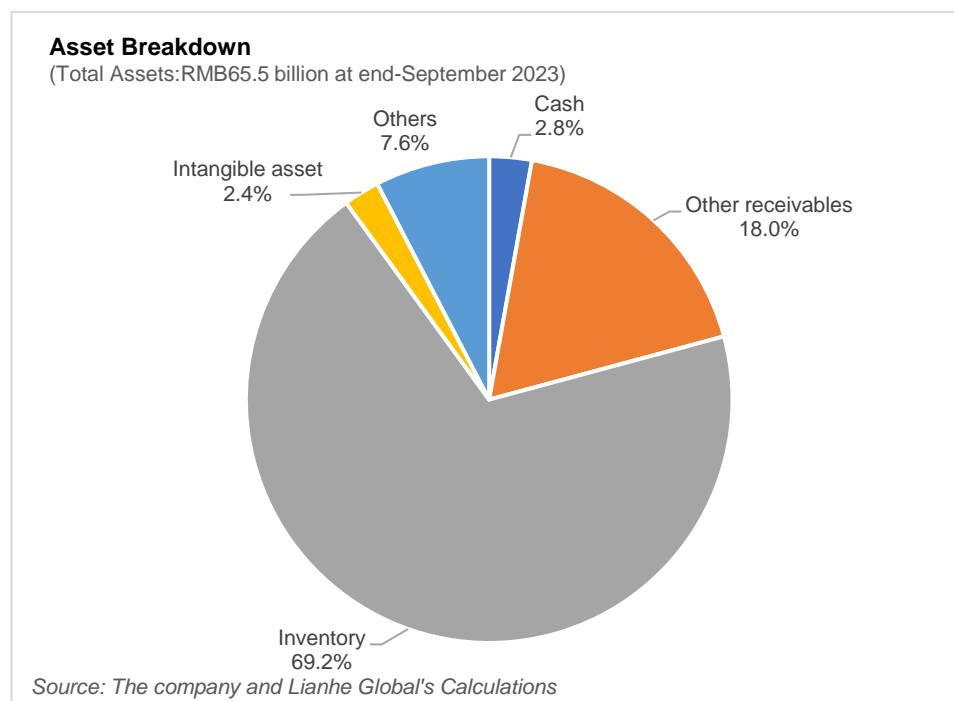
## Financial Profile

### Balance Sheet Structure and Quality

Balance Sheet Structure and Quality				
(RMB million)	2020	2021	2022	Sept. 2023
Total Asset	51,283	57,126	65,387	65,517
Equity	37,259	41,424	43,623	43,218
Debt	11,877	13,480	16,464	15,989
Debt / (Debt + Equity) (%)	24.2	24.6	27.4	27.0
LT Debts	9,019	9,610	11,030	11,397
LT Debt / (LT Debt + Equity) (%)	19.5	18.8	20.2	20.9

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

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collection schedule for construction costs is subject to the local government's fiscal conditions. WHIH's also had many other receivables (primarily due from local SOEs), which amounted to RMB11.8 billion and accounted for 18.0% of total asset. These receivables usually take one to three years to collect. Moreover, WHIH had intangible asset valued at RMB1.6 billion, mainly comprised use right of sea area injected by the local government.

### Debt Servicing Capability

The liquidity of WHIH was tight. At end-September 2023, the company had cash balance of RMB1.8 billion (including restricted cash of RMB1.6 billion), compared with its debt due within one year of RMB4.6 billion. At the same time, the company only had unused bank facilities of RMB778 million. We expect the company to roll over most of its short-term bank borrowings (end-September 2023: c. RMB2.0 billion). Yet obtaining additional financing channels and timely government support are important for WHIH to maintain its liquidity.

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