

Lianhe Global has assigned ‘BBB’ global scale Long-term Issuer Credit Rating with Stable Outlook to Haiyang State-owned Capital Operation Group Co., Ltd.

HONG KONG, 7 February 2024 – Lianhe Ratings Global Limited (“Lianhe Global”), an international credit rating company, has assigned ‘BBB’ global scale Long-term Issuer Credit Rating to Haiyang State-owned Capital Operation Group Co., Ltd. (“HSCOG” or “the company”). The Outlook is Stable.

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

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

Key Rating Rationales

Haiyang Government’s Ownership and Supervision: The Haiyang government holds the full ownership of HSCOG through the Finance Bureau of Haiyang County (“Haiyang FB”). The Haiyang 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 Haiyang 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 Haiyang and Strategic Alignment: HSCOG, as the key LIDC in Haiyang, is primarily responsible for the investment, development and operation of infrastructure projects and shantytowns renovation projects within the city. Serving as the sole entity in charge of infrastructure projects throughout the region, HSCOG is mainly engaged in urban renewal, road construction and upgrading and other infrastructure related projects with strong regional advantages. It is also entrusted with the function of industrial investment and tourism development in Haiyang. HSCOG 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: HSCOG received operational and financial support from the Haiyang government. HSCOG received a total subsidy amount of RMB297.8 million from 2020 to the first nine months of 2023. The Haiyang government continued to inject capital, project-related assets, right of use assets, equities of other companies and other kinds of assets into HSCOG to expand its asset size and diversify its business. Besides, the Haiyang government will repurchase some infrastructure projects and provide policy supports to HSCOG to ensure its business operation. Given that it is the sole entity for infrastructure construction and shantytown renovation in Haiyang, HSCOG has an advantage in acquiring related resources and major projects. We believe HSCOG is likely going to receive government support to support its daily business operation.

HSCOG's Financial and Liquidity Position: HSCOG's total assets showed a continuous growth trend in the past few years and reached RMB30.8 billion at end-September 2023, largely attributed to the increase of inventories that related to the company's infrastructure construction business. The current assets of HSCOG accounted for 61.2% of the total assets at end-September 2023, yet the overall asset liquidity was moderately weak due to large amount of inventories and receivables. HSCOG's financial leverage (total liabilities to total assets) declined to 40.4% and its adjusted debt decreased to RMB7.1 billion at end-September 2023 from RMB8.7 billion at end-2022. The liquidity of HSCOG was tight. At end-September 2023, HSCOG had a cash balance and unused credit facilities of RMB1.8 billion and RMB607.4 million, respectively, compared with its debt due within one year of RMB2.7 billion. Having said that, HSCOG 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 Haiyang: Haiyang is a county-level city of Yantai City, Shandong Province, and is located in the southern end of Jiaodong Peninsula. Haiyang's economic growth fluctuated in the past three years due to the COVID-19 pandemic, with a year-over-year growth rate of -1.5%, 6.0% and 4.5% in 2020, 2021 and 2022, respectively. Haiyang's GDP reached RMB49.8 billion in 2022, and ranked the 7th among all districts and county-level cities under the administration of Yantai. The Haiyang government's aggregate fiscal revenues are mainly derived from budgetary income and government fund income. The Haiyang government's budgetary revenue decreased to c. RMB3.0 billion in 2022 from c. RMB3.1 billion in 2021. In contrast, its budgetary expenditure increased to RMB4.6 billion in 2022 from RMB4.4 billion in 2021. Therefore, the Haiyang government's budget deficit was enlarged to -52.3% over the same period. The debt ratio, as measured by total government debt outstanding/aggregate revenue, had increased to 160.6% at end-2022 from 125.4% at end-2020, mainly due to the increase in special debt.

Rating Sensitivities

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

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

About Lianhe Global

Lianhe Global is an international credit rating company that provides credit ratings to corporations, banks, non-bank financial institutions, local investment and development companies, and other asset classes around the globe. Lianhe Global also provides credit risk research and other services related to credit ratings.

Rating Methodology

The principal methodology used in this HSCOG's rating is Lianhe Global's China Local Investment and Development Companies Criteria published on 5 December 2022, which can be found at the website www.lhratingsglobal.com.

Note: The above Issuer/Issuance Credit Ratings are solicited at the request of the rated entity or a related third party.

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