

Shandong Taifeng Holding Group Co., Ltd.

Initial Issuer Report

Summary

Issuer Rating	BBB-
Outlook	Stable
Location	China
Industry	Local Investment and Development Companies
Date	6 February 2024

Key Figures of SDTF and Xintai

(RMB billion)			
	2021	2022	
Xintai			
GDP	57.4	63.0	
GDP growth rate (%)	5.3	4.4	
Budgetary revenue	3.8	3.5	
Government fund	3.5	2.9	
Transfer payment	2.6	3.0	
Budgetary expenditure	7.6	6.5	
SDTF	2022	2023.9	
Asset	12.5	12.4	
Equity	6.5	6.5	
Revenue	1.4	1.0	

Source: Public information, SDTF and Lianhe Global's calculations

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

Summary

The Issuer Credit Rating reflects a high possibility that the People’s Government of Xintai City (“Xintai government”) would provide very strong support to SDTF if needed, in light of its full ownership of SDTF, SDTF’s strategic importance as an important local investment and development company (“LIDC”) responsible for state-owned asset operation in Xintai City (“Xintai”), and the linkage between the Xintai government and SDTF, 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 Xintai government may face significant negative impact on its reputation and financing activities if SDTF encounters any operational and financial difficulties.

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

Rating Rationale

Xintai Government’s Ownership and Supervision: The Xintai government holds 100% ownership of SDTF through the Xintai State-owned Assets Operation Center (“Xintai SAOC”). As the ultimate controller of SDTF, Xintai government has strong control and supervision over the company, including management appointment, decision on its strategic development and investment plan and supervision of its major funding decisions. In addition, the Xintai government has assessment mechanism over the company through Xintai SAOC and appoints auditors to supervise the operating performance and financials on a periodic basis.

Strategic Importance to Xintai and Strategic Alignment: SDTF is an important LIDC responsible for state-owned assets operation in Xintai. The company runs coal mine, tree farm, reservoir and an array of state-owned properties within the region. The company’s business operation plays a significant role in value maintenance and appreciation of state-owned assets, job creation and tax contribution in Xintai. Its strategic planning has been aligned with the local government’s economic and social development plans.

Ongoing Government Support: SDTF receives ongoing support from the local government. The Xintai government provided financial support of RMB953 million between 2020 and 2023 to SDTF to support its operations. The local government also arranged Xintai Integrated Urban-Rural Development Co., Ltd., (“XIURD”) another LIDC mainly responsible for project development in Xintai, to guarantee SDTF’s bank borrowings and bond issuances, enhancing SDTF’s financing capability. We expect the support from the local government to remain intact given SDTF’s strategic importance in Xintai.

Economy and Fiscal Condition of Xintai: Xintai is a county-level city under the jurisdiction of Shandong Province and managed by Tai’an City (“Tai’an”). Xintai maintained a relatively stable GDP growth between 2020 and 2022, reaching RMB63.0 billion in 2022. Its economic

Analysts

Sigmund Jiang, CFA, CESGA
 (852) 3462 9587
sigmund.jiang@lhratingsglobal.com

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

Applicable Criteria

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

development focused on equipment manufacturing, fine chemicals, new energy and optoelectronic technology industry in recent years.

The Xintai government's budgetary revenue was on a downward trend, lowering to RMB3.5 billion in 2022 from RMB4.1 billion in 2021. The fiscal self-sufficiency rate of the Xintai government was low, recording budget deficit 84.8% in 2022. Yet the Xintai government continuously received a certain number of subsidies from higher government authorities.

Xintai's government fund income, mainly generated by land sales, declined to RMB2.9 billion in 2022 from RMB3.5 billion in 2021, mainly owing to the weak property market. However, the outstanding debt of the Xintai government continued to grow, as the Xintai government borrowed heavily in special debts to support its public projects. Its fiscal debt ratio, as measured by total government debt outstanding/aggregate revenue, surged to 139.3% at end-2022 from 79.9% at end-2020.

SDTF's Financial and Liquidity Position: SDTF's total asset was on a downward trend in the past few years, decreasing to RMB12.4 billion at end-September 2023 from RMB13.3 billion at end-2020. Its total debt also decreased to RMB2.8 billion from RMB3.3 over the same period. Therefore, the company's financial leverage, as measured by debt/capitalization, stayed at a manageable level of around 30%.

However, SDTF's asset quality is moderately weak, as the company had a large number of other receivables, which accounted for 41.8% of total asset at end-September 2023. They were primarily due from local government agencies and SOEs, usually without a specified repayment schedule. The local government agencies' repayment is highly subject to the fiscal conditions of the local government.

The liquidity of SDTF was tight. At end-September 2023, the company had cash balance of RMB527 million (including restricted cash of RMB420 million), while it had debt due within one year of RMB1.4 billion. The company has access to various financing channels, including bank borrowings and bond issuances to support its operations and debt repayments. Yet it only had unused bank facilities of RMB83 million at end-September 2023. It is vital for SDTF to refinance its incoming maturities and obtain timely support from the local government.

High Contingent Liability: SDTF's contingent liability is high. The company provided financial guarantees of RMB2.5 billion to third parties at end-September 2023, accounting for 38.2% of its net assets. Guaranteed parties were mainly other SOEs (including XIURD) and some private-owned companies in Xintai. The reciprocal guarantees between SDTF and XIURD, two major bond issuance entities in Xintai, also indicate a significant contagion risk among LIDCs and SOEs within the region.

Rating Sensitivities

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

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

Operating Environment

Economic Condition of Xintai

Xintai is a county-level city under the jurisdiction of Shandong Province and managed by Tai'an. It is located in the southeastern part of Tai'an. Xintai has a total land area of 1,946 square kilometers and a resident population of 1.25 million, with an urbanization rate of 61.1%.

Xintai maintained a relatively stable economic growth between 2020 and 2022, with moderate GDP growth rates of 3.6%, 5.3% and 4.4% in 2020, 2021 and 2022, respectively. Its GDP reached RMB63.0 billion in 2022. Yet the GDP per capita was RMB50,000 in 2022, lower than that of Tai'an (RMB59,000) as well as that of China (RMB85,700).

Xintai's economic growth was mainly fueled by the secondary and tertiary industries in the past few years, which accounted for 42.5% and 46.7% of GDP in 2022, respectively. Its economic development focused on equipment manufacturing, fine chemicals, new energy and optoelectronic technology industry in recent years.

Xintai's GDP and Fixed Asset Investment			
(RMB billion)	2020	2021	2022
GDP	52.2	57.4	63.0
-Primary industry (%)	11.1	11.0	10.8
-Secondary industry (%)	38.8	40.0	42.5
-Tertiary industry (%)	50.2	49.1	46.7
GDP growth rate (%)	3.6	5.3	4.4
Fixed asset investment growth rate (%)	7.1	-44.3	20.9
Population (million)	1.27	1.26	1.25

Source: Public information and Lianhe Global's calculations

Fiscal Condition of Xintai

The Xintai government's budgetary revenue was on a downward trend, lowering to RMB3.5 billion in 2022 from RMB3.8 billion in 2021 and RMB4.1 billion in 2020. The tax revenue accounted for 60.9% of the budgetary revenue in 2022, down from 70.6% in 2021, mainly due to related tax-advantaged policies. The fiscal self-sufficiency rate of the Xintai government was low, recording budget deficit of 76.2%, 102.9% and 84.8% in 2020, 2021 and 2022, respectively. Yet the Xintai government continuously received a certain number of subsidies from higher government authorities.

As another substantial component of the local fiscal revenue, Xintai's government fund income, mainly generated by land sales, declined to RMB2.9 billion in 2022 from RMB3.5 billion in 2021, mainly owing to the weak property market. However, the outstanding debt of the Xintai government continued to grow. At end-2022, the Xintai government's outstanding debt was RMB13.3 billion, as the Xintai government borrowed heavily in special debts to support its public projects. Its fiscal debt ratio, as measured by total government debt outstanding/aggregate revenue, surged to 139.3% at end-2022 from 79.9% at end-2020.

Xintai's Fiscal Condition			
(RMB billion)	2020	2021	2022
Budgetary revenue	4.1	3.8	3.5
Budgetary revenue growth rate (%)	0.6	-8.3	-5.5
Tax revenue	2.4	2.6	2.2

Tax revenue (% of budgetary revenue)	58.0	70.6	60.9
Government fund income	5.0	3.5	2.9
Transfer payment	2.9	2.6	3.0
Aggregate revenue	12.0	9.9	9.5
Budgetary expenditure	7.2	7.6	6.5
Budget balance ¹ (%)	-76.2	-102.9	-84.8

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

Source: Public information and Lianhe Global's calculations

Ownership Structure

Government's Ownership

SDTF was established in March 1996 with an initial registered capital of RMB28 million, funded by Coal Management Bureau of Xintai. After a series of capital increases and equity transfers, SDTF's registered capital and paid-in capital were both RMB44.8 million at end-June 2023; Xintai SAOC, as the sole controlling shareholder, held 100% of the company's equity. The actual controller of the company is the Xintai government.

Strategic Importance and Government Linkage

Strategic Importance of SDTF to Xintai

SDTF is an important LIDC responsible for state-owned assets operation in Xintai. The company runs coal mine, tree farm, reservoir and an array of state-owned properties within the region. The company's business operation plays a significant role in value maintenance and appreciation of state-owned assets, job creation and tax contribution in Xintai. Its strategic planning has been aligned with the local government's economic and social development plans.

Strong Linkage with the Local Government

SDTF's linkage with the local government is strong as the Xintai government holds 100% ownership of SDTF through the Xintai SAOC. The Xintai government has strong control and supervision over the company, including management appointment, decision on its strategic development and investment plan and supervision of its major funding decisions. In addition, the Xintai government has assessment mechanism over the company through Xintai SAOC and appoints auditors to supervise the operating performance and financials on a periodic basis.

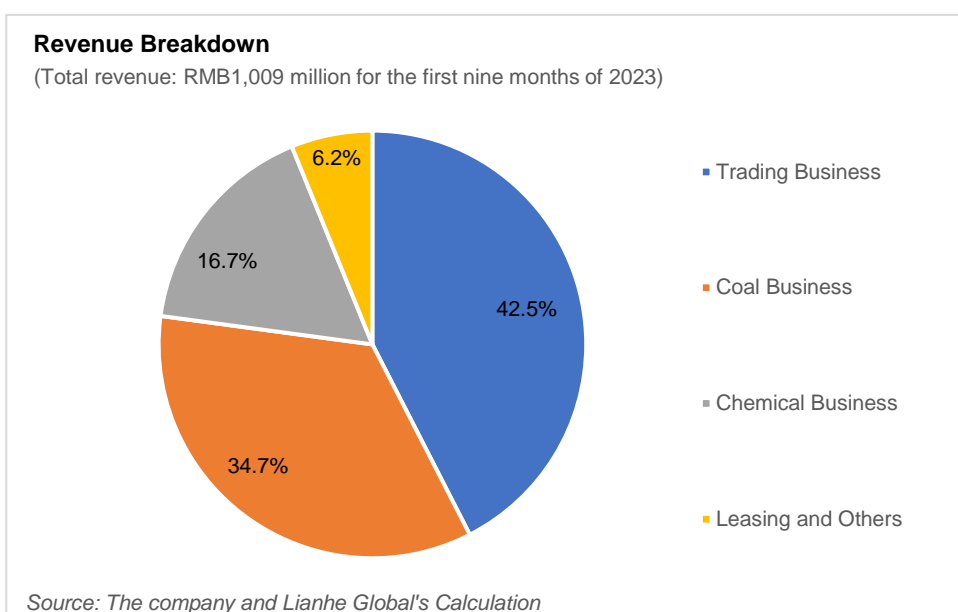
Ongoing Government Support

SDTF receives ongoing support from the local government. The Xintai government provided financial support of RMB381 million, 190 million, 191 million and 190 million in 2020, 2021, 2022 and 2023 to SDTF to support its operations. The local government also arranged XIURD, another LIDC mainly responsible for project development in Xintai, to guarantee SDTF's bank borrowings and bond issuances, enhancing SDTF's financing capability. We expect the support from the local government to remain intact given SDTF's strategic importance in Xintai.

Business Profile

An Important LIDC Responsible for State-owned Assets Operation in Xintai

SDTF is an important state-owned assets operation entity in Xintai, operating a coal mine, tree farm, reservoir and an array of state-owned properties. The company also engages in chemical and trading businesses. SDTF realized total revenue of RMB976 million, 1,505 million, 1,405 million and 1,009 million in 2020, 2021, 2022 and the first nine months of 2023, respectively. The overall gross profit margin of SDTF fluctuated between around 10%- 20% over the same period.



Coal Business

SDTF operates Wangjiazhai Coal Mine with annual production capacity of 750,000 tons in Xintai and Datonggou Coal Mine with annual production capacity of 600,000 tons in Heilongjiang Province's Jixi City. The company mainly adopts long-term contracts and spot sales models, supplying coals for thermal power, coal trading companies, coal washing and preparation and other and other energy consuming enterprises in neighboring regions.

The revenue derived from this segment amounted to RMB235 million, 371 million, 362 million and 350 million in 2020, 2021, 2022 and the first nine months of 2023, respectively. The gross margin has remained at a relatively high level of 40%-50% since 2021, owing to the high coal prices. However, the profitability of coal business is susceptible to uncertainties arising from factors such as policy, market and downstream industries.

Trading Business

SDTF's trading segment mainly engages in the sales of coal, steel and ethanediol etc. The company's trading business is conducted in a "direct shipping and sales" model, where the company enters into a sales contract with the customer and then signs a purchase contract with a qualified supplier, and the suppliers will send traded goods directly to the customers. Finally, the company settles with the customers and the suppliers, respectively. Trading segment was the largest source of revenue for SDTF. However, its gross margin was very

low, recording 0.38% in the first nine months of 2023. Moreover, the segment has a high concentration of buyers, mainly small and medium-sized private enterprises, indicating a relatively high counterparty risk.

Chemical, Leasing and Others

SDTF has 51% stake in Shandong Feiyang Chemical Co., Ltd. ("Feiyang Chemical"), a state-owned chemical plant in Xintai. Feiyang Chemical mainly produces and sells chemical materials such as succinic acid, dimethyl carbonate and propylene glycol, etc. In addition, SDTF participates in the leasing of state-owned properties and other businesses, with each accounting for a relatively small proportion of the company's total revenue.

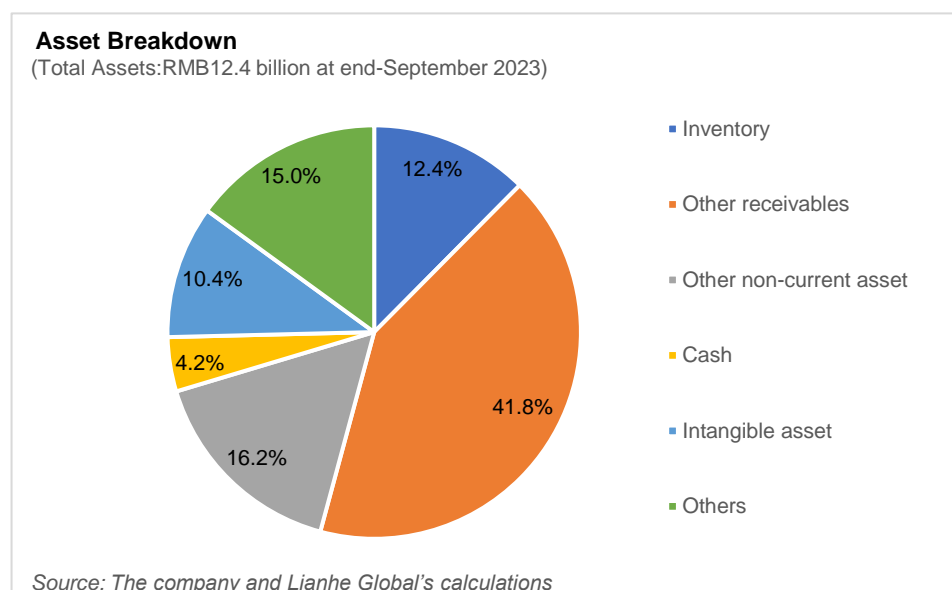
Financial Profile

Balance Sheet Structure and Quality

Balance Sheet Structure and Quality				
(RMB million)	2020	2021	2022	September 2023
Total Asset	13,260	12,823	12,470	12,411
Equity	6,457	6,355	6,451	6,534
Debt	3,313	2,899	2,812	2,780
Debt / (Debt + Equity) (%)	33.9	31.3	30.4	29.8
LT Debts	1,701	1,388	1,101	1,339
LT Debt / (LT Debt + Equity) (%)	20.9	17.9	14.6	17.0

Source: Company information and Lianhe Global's calculations

SDTF's total asset was on a downward trend in the past few years, decreasing to RMB12.4 billion at end-September 2023 from RMB13.3 billion at end-2020. Its total debt also decreased to RMB2.8 billion from RMB3.3 over the same period. Therefore, the company's financial leverage, as measured by debt/capitalization, stayed at a manageable level of around 30%.



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repayment schedule. The local government agencies' repayment is highly subject to the fiscal conditions of the local government. In addition, the company had sizable inventory (mainly land use rights) and intangible asset (mainly land use rights and mining rights), which added up to RMB2.8 billion at end-September 2023, representing 22.8% of total asset.

Debt Servicing Capability

The liquidity of SDTF is tight. At end-September 2023, the company had cash balance of RMB527 million (including restricted cash of RMB420 million), while it had debt due within one year of RMB1.4 billion. The company has access to various financing channels, including bank borrowings and bond issuances to support its operations and debt repayments. Yet it only had unused bank facilities of RMB83 million at end-September 2023. It is vital for SDTF to refinance its incoming maturities and obtain timely support from the local government.

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