

# Danjiangkou Jiaotou Yuantu Materials Co. Ltd.

## Initial Issuer Report

### Summary

<b>Issuer Rating</b>	BBB-
<b>Outlook</b>	Stable
<b>Location</b>	China
<b>Industry</b>	Local Investment and Development Companies
<b>Date</b>	19 March 2024

### Key Figures of Danjiangkou and DJYM (RMB billion)

	2021	2022
Danjiangkou		
GDP	30.2	35.0
GDP growth rate (%)	11.4	9.8
Budgetary revenue	1.2	1.6
Government fund	1.5	1.3
Transfer payment	3.5	3.5
Budgetary expenditure	4.8	5.4
DJYM	<b>2022</b>	<b>2023</b>
Assets	1.7	11.4
Equity	0.4	6.9
Revenue	0.56	1.45

Source: Public information, DJYM 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 Danjiangkou Jiaotou Yuantu Materials Co. Ltd. (“DJYM” or “the company”)

### Summary

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

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

### Rating Rationale

**Danjiangkou Government’s Ownership and Supervision:** The Danjiangkou government holds the full ownership of DJYM through the Finance Bureau of Danjiangkou City’s (“Danjiangkou FB”) fully-owned subsidiary, Danjiangkou Transportation Investment Co. Ltd. (“DTI”). The Danjiangkou 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 Danjiangkou 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 Danjiangkou and Strategic Alignment:** DJYM, as the key LIDC in Danjiangkou, is the sole entity responsible for mining and quarrying of minerals and sand. It holds government-authorized franchise rights with the aim of establishing a high-standard sand and gravel transportation center. Leveraging the sand and gravel transportation center, the company is developing a green building material industrial park and supplying sand, gravel and other materials to other entities in Danjiangkou. Additionally, the company is responsible for selling greenery and maintenance services for municipal infrastructure facilities, stations and service zone projects. The company is also involved in the development of tourism and some transportation-related infrastructure construction projects in Danjiangkou. DJYM 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:** DJYM received operational and financial support from the Danjiangkou government. DJYM received a total subsidy amount of RMB717.1 million from 2021 to 2023. The Danjiangkou government continued to inject capital, right of use assets, equities of other companies and other kinds of assets into DJYM to expand its asset size

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### Applicable Criteria

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

and diversify its business. Besides, the Danjiangkou government will provide policy support to the company to ensure the operation of its business. Given that it is the sole entity for gravel, sand and greenery supply in Danjiangkou, DJYM has an advantage in acquiring related resources and major projects. We believe DJYM is likely going to receive government support to support its daily business operation.

**DJYM's Financial Matrix and Liquidity Position:** DJYM's total assets showed a continuous growth trend in the past few years and reached RMB11.4 billion at end-2023, largely attributed to the consolidation of two subsidiaries. The current assets of DJYM accounted for 39.1% of the total assets at end-2023, and the overall asset liquidity was moderately weak due to large amount of intangible asset, inventory and account receivables. These assets usually take a long time to monetize due to the protracted construction and payment collection period.

DJYM's financial leverage (total liabilities to total assets) rapidly declined to 39.2% at end-2023 from 76.7% at end-2021 with the equity injection of other companies from the Danjiangkou government. Its adjusted debt decreased to RMB1,171 million at end-2023 from RMB1,243 million at end-2021. DJYM's liquidity was sufficient. At end-2023, DJYM had a cash balance of RMB92 million, compared with its debt due within one year of RMB45.4 million. Besides, DJYM has access to various financing channels, including bank loans and non-traditional financing, to support its debt repayment and business operations.

**Economy and Fiscal Strength of Danjiangkou:** Danjiangkou is a county-level city under the jurisdiction of Shiyang City. After a slump of 7.3% in 2020 due to covid's disruption, Danjiangkou's economic growth had rebounded significantly since 2021, with its GDP growth at 11.4% and 9.8% in 2021 and 2022, respectively. Danjiangkou's economic growth was mainly fueled by the secondary industry and tertiary industries in the past few years, which accounted for 38.7% and 49.8% of the GDP in 2022, respectively.

Danjiangkou's budgetary revenue increased steadily to RMB1.6 billion in 2022 from RMB0.9 billion in 2020, with the contribution of the tax revenue elevated to 82.5% from 62.0% over the same period. The fiscal self-sufficiency rate of the Danjiangkou government was relatively low (29% in 2022) and it recorded a budget deficit of 243.2% in 2022. Therefore, the Danjiangkou government continuously received a certain number of subsidies from higher government authorities. In addition, Danjiangkou's government fund income fluctuated between RMB0.7 billion in 2020 and RMB1.3 billion in 2022, mainly due to the fluctuation of land use right transfer income amid challenging property market conditions. Given the Danjiangkou government borrowed heavily in special debts to support its public projects, its fiscal debt ratio, as measured by total government debt outstanding/aggregate revenue, increased to 84.5% at end-2022 from 64.9% at end-2020.

### Rating Sensitivities

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

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

## Operating Environment

### Economic Condition of Danjiangkou

Danjiangkou is a county-level city under the direct jurisdiction of Hubei Province and administered by Shiyan City. Danjiangkou is a time-honored city with abundant tourism resources and cultural sites, and is the core water source area of the South-to-North Water Diversion Project. Danjiangkou has jurisdiction over 12 towns, 4 streets, 3 forestry development management area, one economic development management office and one tourism special economic zone, with a land area of 3,121 square kilometers. At end-2022, Danjiangkou had a resident population of c. 0.4 million, with an urbanization rate of 63.9%.

After a slump of 7.3% in 2020 due to covid's disruption, Danjiangkou's economic growth had rebounded significantly since 2021, with its GDP growth at 11.4% and 9.8% in 2021 and 2022, respectively. Danjiangkou's economic growth was mainly fueled by the secondary industry and tertiary industries in the past few years, which accounted for 38.7% and 49.8% of the GDP in 2022, respectively. Its economic development focused on tourism, automobile and equipment manufacturing, water resources and processing of agricultural products, new energy and new materials industry in recent years. Its fixed asset investment growth rate fluctuated in the past few years, which was c. -49.4%, 28.4% and 33.7% in 2020, 2021 and 2022, respectively.

#### Danjiangkou's GDP and Fixed Asset Investment

(RMB billion)	2020	2021	2022
GDP	27.0	30.2	35.0
-Primary industry (%)	12.4	12.3	11.5
-Secondary industry (%)	39.0	32.8	38.7
-Tertiary industry (%)	48.6	54.9	49.8
GDP growth rate (%)	-7.3	11.4	9.8
Fixed asset investment	9.5	12.2	15.6
Fixed asset investment growth rate (%)	-49.4	28.4	33.7
Population (million)	0.4	0.4	0.4

Source: Public information and Lianhe Global's calculations

### Fiscal Condition of Danjiangkou

Danjiangkou's budgetary revenue increased steadily to RMB1.6 billion in 2022 from RMB0.9 billion in 2020, with the contribution of the tax revenue elevated to 82.5% from 62.0% over the same period. The fiscal self-sufficiency rate of the Danjiangkou government was relatively low (c. 29% in 2022) and it recorded a budget deficit of 243.2% in 2022. Therefore, the Danjiangkou government continuously received a certain number of subsidies from higher government authorities, and the transfer payment recorded at RMB3.5 billion in 2022. In addition, Danjiangkou's government fund income fluctuated between RMB0.7 billion in 2020 and RMB1.3 billion in 2022, mainly due to the fluctuation of land use right transfer income amid challenging property market conditions.

The outstanding debt of the Danjiangkou government continued to grow. At end-2022, the Danjiangkou government's outstanding debt was c. RMB5.4 billion, including RMB2.8 billion of general obligations and RMB2.6 billion of special debt. Given the Danjiangkou government borrowed heavily in special debts to support its public projects, its fiscal debt ratio, as measured by total government debt outstanding/aggregate revenue, had increased to 84.5% at end-2022 from 64.9% at end-2020.

#### Danjiangkou's Fiscal Condition

(RMB billion)	2020	2021	2022
Budgetary revenue	0.9	1.2	1.6

Budgetary revenue growth rate (%)	-27.1	37.1	27.0
Tax revenue	0.6	0.9	1.3
Tax revenue (% of budgetary revenue)	62.0	68.1	82.5
Government fund income	0.7	1.5	1.3
Transfer payment	4.6	3.5	3.5
<b>Aggregate revenue</b>	<b>6.2</b>	<b>6.3</b>	<b>6.4</b>
Budgetary expenditure	5.7	4.8	5.4
Budget balance <sup>1</sup> (%)	-530.7	-281.2	-243.2

<sup>1</sup> Budget balance = (1-budgetary expenditure / budgetary revenue) \* 100%

Source: Public information and Lianhe Global's calculations

## Ownership Structure

### Government's Ownership

DJYM was established by the DTI in May 2019, with a registered capital of RMB0.1 billion. At end-2023, DJYM's registered and paid-in capital were both at RMB0.1 billion. DJYM had a shareholding structure in which the DTI, as the controlling shareholder, held 100% of the company's equity.

## Strategic Importance and Government Linkage

### Strategic Importance of DJYM to Danjiangkou

DJYM, as the key LIDC in Danjiangkou, is the sole entity responsible for mining and quarrying of minerals and sand. It holds government-authorized franchise rights with the aim of establishing a high-standard sand and gravel transportation center. Leveraging the sand and gravel transportation center, the company is developing a green building materials industrial park and supplying sand, gravel, and other materials to other entities in Danjiangkou. Additionally, the company is responsible for selling greenery and maintenance services to municipal infrastructure, stations, service area projects, and is involved in the development of tourism and some transportation-related infrastructure construction projects in Danjiangkou. DJYM 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.

### Strong Linkage with the Local Government

DJYM's linkage with the local government is strong as the Danjiangkou government holds the full ownership of DJYM through Danjiangkou FB's fully-owned subsidiary DTI. The Danjiangkou 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 Danjiangkou 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

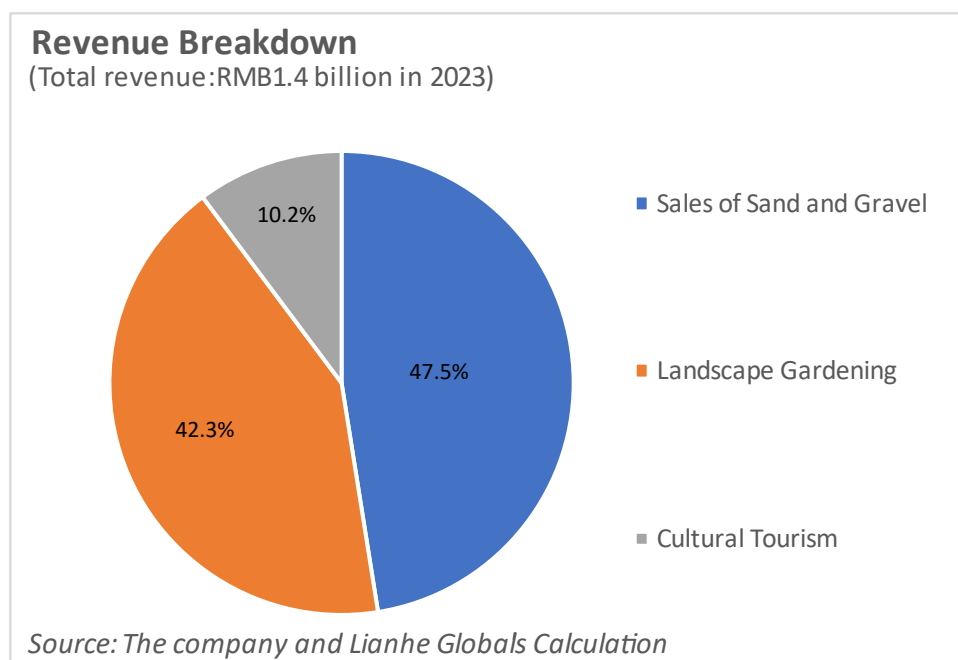
DJYM received operational and financial support from the Danjiangkou government. DJYM received a total subsidy amount of RMB717.1 million from 2021 to 2023. The Danjiangkou government continued to inject capital, right of use assets, equities of other companies and other kinds of assets into DJYM to expand its asset size and diversify its business. Besides, the Danjiangkou government will provide policy support to the company to ensure the operation of its business. Given that it is the sole entity for gravel, sand and greenery supply

in Danjiangkou, DJYM has an advantage in acquiring related resources and major projects. We believe DJYM is likely going to receive government support to support its daily business operation.

## Business Profile

### The Key Entity Responsible for State-owned Assets Operation in the Danjiangkou

DJYM, as a key LIDC in the Danjiangkou, mainly is responsible for mining and operation of sand and gravel within the region. The primary sources of operating revenue for DJYM are sand and gravel sales, landscape gardening and cultural tourism. The company's total revenue surged to RMB1.4 billion in 2023 from RMB60 million in 2021, mainly due to the consolidation of two subsidiaries. The overall gross profit margin of DJYM fluctuated between 17.5% and 75.7% over the same period. In general, DJYM's business was concentrated, and it has regional advantages in its major businesses.



### Sales of Sand and Gravel

As an important source of revenue for the company, the sales of sand and stone segment have become DJYM's largest source of revenue since 2021. DJYM is mainly engaged in the merchandise sales of sand and gravel, and follows the market environment to determine the purchase price and sell price. The revenue generated from this segment reached c. RMB59.3 million, RMB54.2 million and RMB0.7 billion in 2021, 2022 and 2023, respectively, representing an upward trend in 2023. The gross profit margin of this segment declined rapidly to 17.6% in 2023 from 76.6% in 2021.

### Landscape Gardening

The company undertakes landscaping construction and municipal facilities management within the region. The company started landscape gardening business in 2023, and the revenue of this segment was RMB0.6 billion, with a low gross profit margin (c. 3.6%).

### Cultural Tourism

The company undertakes cultural tourism projects within the region. The revenue of this segment rapidly increased to RMB148 million in 2023 from RMB0.3 million in 2021. The gross profit margin of this segment remained negative in 2021 and 2022, but surged to 74.8% in 2023.

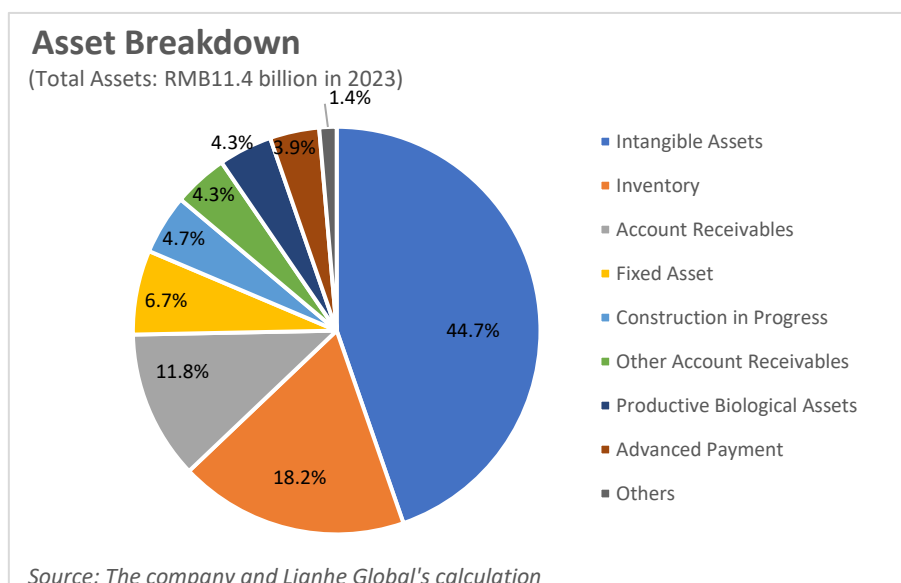
## Financial Profile

### Balance Sheet Structure and Quality

Balance Sheet Structure and Quality			
(RMB million)	2021	2022	2023
Total Asset	1,748	1,704	11,369
Equity	408	433	6,912
Debt	1,243	1,220	1,171
Debt / (Debt + Equity) (%)	75.3	73.8	14.5
LT Debt	1,137	1,121	1,126
LT Debt / (LT Debt + Equity) (%)	73.6	72.1	14.0

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

DJYM's total asset size surged to RMB11.4 billion at end-2023 from RMB1.7 billion at end-2021, largely attributed to the consolidation of two subsidiaries. The company's financial leverage, as measured by total liability/total asset, rapidly declined to 39.2% at end-2023 from 76.7% at end-2021. Its debt structure was improving, with long-term debt's proportion increased to 96.1% at end-2023. Therefore, the company's short-term debt pressure was largely decreased. The total adjusted debt decreased to RMB1.17 billion at end-2023 from RMB1.24 billion at end-2021.



DJYM's assets liquidity was weak. At end-2023, the company's assets mainly consisted of intangible asset, inventory and account receivables, which added up c. RMB 8.5 billion at end-2023, representing c. 74.7% of total asset. The company had a large size of intangible

asset (mainly use rights of sea area and land as well as franchise rights), which amounted to c. RMB5.1 billion at end-2023, representing 44.7% of total asset. The company's project construction activities accumulated sizeable inventories (mainly lands and construction costs), fixed asset and construction in progress, totally amounting to RMB3.4 billion, representing 29.6% of total asset at end-2023. These assets usually take a long time to monetize due to the protracted construction and payment collection period. In addition, the company had a large number of account receivables, primarily due from government agencies, representing 11.8% of total asset at end-2023. Their repayment schedules are highly subject to the fiscal conditions of the local government.

### Debt Servicing Capability

DJYM's liquidity was sufficient. At end-2023, DJYM had a cash balance of RMB92 million, compared with its debt due within one year of RMB45.4 million. Besides, DJYM 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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