

## Hubei Sanjiang Industrial Investment Co., Ltd.

### Initial Issuer Report

#### Summary

Issuer Rating	BBB
Outlook	Stable
Location	China
Industry	Local Investment and Development Companies
Date	5 July 2024

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

#### Summary

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

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

#### Rating Rationale

**Government’s Ownership and Supervision:** HSII is the core subsidiary of Yidu Guotong Investment Development Co., Ltd. (“YGID”), a key LIDC which 89.95% shares are ultimately owned by Yidu State-owned Asset Supervision and Administration Bureau (“Yidu SASAB”). Yidu SASAB is HSII’s actual controller. The Yidu government has strong supervision over the company, including management appointment, decision on its strategic development, and supervision of its major investment and funding plans. In addition, the local government has assessment mechanism over the company and appoints auditors to supervise its operating performance and financials on a periodic basis.

**Strategic Importance and Alignment:** HSII is an important LIDC responsible for project construction and industrial operation in Yidu. The company mainly develops and operates industrial parks and scenic spots in Yidu to promote local industries and tourism development, which are aligned with the Yidu government’s economic and social development plans. The company also engages in properties sales, building materials, water supply and leasing businesses.

**Government Support:** The Yidu government provides support to HSII. Between 2021 and 2023, the Yidu government injected assets such as mining rights, use rights of forest and equity of other local SOEs, totally valued at RMB3.5 billion, into HSII. Over the same period, the company received operational subsidies from the local government. We expect the support from the local government to remain intact given HSII’s strategic importance in Yidu.

**Economy and Fiscal Condition of Yidu:** Yidu is a county-level city directly under the jurisdiction of Hubei Province and managed by Yichang City. It is listed as Top 100 Counties in China in 2022, with a good industrial development. Yidu maintained rapid economic growth in the past three year, with growth rates recording at 19.7%, 7.6% and 7.2% in 2021,

#### Key Figures of HSII and Yidu

(RMB billion)

Yidu	2022	2023
GDP	90.0	92.1
GDP growth rate (%)	7.6	7.7
Budgetary revenue	2.3	3.0
Government fund	1.6	1.4
Transfer payment	2.3	2.7
Budgetary expenditure	4.8	5.7
HSII	2023	2024.3
Asset	21.7	22.2
Equity	12.2	12.2
Revenue	1.84	0.32

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

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#### Applicable Criteria

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

2022 and 2023, respectively. Yidu's GDP reached RMB92.1 billion in 2023, which was ranked 1st among 13 districts and counties under the jurisdiction of Yichang.

The Yidu government's budgetary revenue increased rapidly to RMB3.0 billion in 2023 from RMB2.0 billion in 2021, while Transfer payment from higher governments also increased steadily to RMB2.7 billion from RMB2.1 billion. However, the fiscal self-sufficiency of Yidu government was weak and it recorded a budget deficit of 91.4% in 2023. Moreover, Yidu's government fund income decreased to RMB1.4 billion in 2023 from RMB1.6 billion in 2021 amid weak property market.

The outstanding debt of the Yidu government continued to grow due to the new issuance of special debts to support public project development. At end-2023, the Yidu government's outstanding debt increased to RMB8.2 billion from RMB6.4 billion at end-2021. Its fiscal debt ratio, as measured by total government debt outstanding/aggregate revenue, increased to 123.5% at end-2022 from 110.8% at end-2021, then dropped to 116.0% at end-2023, mainly due to the larger increase in aggregate revenue.

**HSII's Financial and Liquidity Position:** HSII's total asset increased steadily to RMB22.2 billion at end-March 2024 from RMB17.2 billion at end-2021, owing to the company's active participation in Yidu's project construction and operation, as well as the asset injection. Its total debt reached RMB5.8 billion at end-March 2024, which was 62.9% higher than that at end-2021 (RMB3.6 billion). Yet its financial leverage, as measured by debt/capitalization, stayed large stable at a manageable level of 30%-35%.

HSII's asset liquidity was relatively weak. The company had a large amount (RMB7.0 billion) of intangible assets (mainly use rights of land and water area as well as sand mining rights injected by local government. Moreover, HSII's project development activities accumulated significant project related assets, which usually take a long time to monetize owing to protracted construction and payment collection periods.

The short-term debt servicing pressure of HSII was moderately high. At end-March 2024, the company had cash balance of RMB1.69 billion (including restricted cash of RMB0.95 billion), while it had debt due within one year of RMB2.40 billion. The company mainly relied on bank borrowings and other non-traditional financings to support its debt repayments and business operations. At end-March 2024, the company had unused credit line of RMB598 million.

## Rating Sensitivities

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

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

## Operating Environment

### Economic Condition of Yidu

Yidu is a county-level city directly under the jurisdiction of Hubei Province and managed by Yichang City. Yidu is located in the southwestern part of Hubei Province, bordering Yangtze River to the northeast, with a total area of 1,357 square kilometers. At end-2023, Yidu had a resident population of 0.4 million, with an urbanization rate of 61.5%. Yidu is listed as Top 100 Counties in China in 2022, with a good industrial development.

Yidu maintained rapid economic growth in the past three year, with growth rates recording at 19.7%, 7.6% and 7.2% in 2021, 2022 and 2023, respectively. Yidu's GDP reached RMB92.1 billion in 2023, which was ranked 1<sup>st</sup> among 13 districts and counties under the jurisdiction of Yichang. Yidu's GDP per capita reached RMB257,000 in 2023, which was well above the Hubei's 95,500.

<b>Yidu's GDP and Fixed Asset Investment</b>			
<b>(RMB billion)</b>	<b>2021</b>	<b>2022</b>	<b>2023</b>
GDP	80.0	90.0	92.1
-Primary industry (%)	8.0	7.9	8.0
-Secondary industry (%)	48.8	53.3	48.4
-Tertiary industry (%)	43.2	38.8	43.6
GDP growth rate (%)	19.7	7.6	7.2
Fixed asset investment growth rate (%)	28.0	23.6	9.9
Population (million)	0.4	0.4	0.4

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

### Fiscal Condition of Yidu

The Yidu government's aggregate fiscal revenues are mainly derived from budgetary revenue and transfer payment from higher government authorities. The Yidu government's budgetary revenue increased rapidly to RMB3.0 billion in 2023 from RMB2.0 billion in 2021, with tax revenue accounting for 78%-82% of budgetary revenue over the same period. Transfer payment from higher governments also increased steadily to RMB2.7 billion from RMB2.1 billion over the same period. However, the fiscal self-sufficiency of Yidu government was weak and it recorded a budget deficit of 91.4% in 2023. Moreover, Yidu's government fund income decreased to RMB1.4 billion in 2023 from RMB1.6 billion in 2021 amid weak property market.

The outstanding debt of the Yidu government continued to grow due to the new issuance of special debts to support public project development. At end-2023, the Yidu government's outstanding debt increased to RMB8.2 billion from RMB6.4 billion at end-2021. Its fiscal debt ratio, as measured by total government debt outstanding/aggregate revenue, increased to 123.5% at end-2022 from 110.8% at end-2021, then dropped to 116.0% at end-2023, mainly due to the larger increase in aggregate revenue.

<b>Yidu 's Fiscal Condition</b>			
<b>(RMB billion)</b>	<b>2021</b>	<b>2022</b>	<b>2023</b>
Budgetary revenue	2.0	2.3	3.0
Budgetary revenue growth rate (%)	36.2	12.6	33.4
Tax revenue	1.6	1.8	2.4
Tax revenue (% of budgetary revenue)	81.9	80.9	78.3
Government fund income	1.6	1.6	1.4
Transfer payment	2.1	2.3	2.7
<b>Aggregate revenue</b>	<b>5.7</b>	<b>6.2</b>	<b>7.1</b>
Budgetary expenditure	3.9	4.8	5.7
Budget balance <sup>1</sup> (%)	-97.3	-114.1	-91.4

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

Source: Public information and Lianhe Global's calculations

## Ownership Structure

### Government's Ownership

HSII was established in May 2010 with a registered capital of RMB5 million. It is the core subsidiary of YGID, a key LIDC in Yidu. Yidu SASAB, as the actual controller, indirectly owns 89.95% shares of the company.

## Strategic Importance and Government Linkage

### Strategic Importance of HSII to Yidu District

HSII is an important LIDC responsible for project development in Yidu. The company mainly develops and operates industrial parks and scenic spots in Yidu to promote local industries and tourism development, which are aligned with the Yidu government's economic and social development plans. The company also engages in properties sales, building materials, water supply and leasing businesses.

### Strong Linkage with the Local Government

HSII's linkage with the Yidu government is strong. Yidu SASAB indirectly owns 89.95% shares of the company and is the company's actual controller. The Yidu government has strong control and supervision over the company, including management appointment, decision on its strategic development, and supervision of its major investment and funding plans. In addition, the local government has assessment mechanism over the company and appoints auditors to supervise its operating performance and financials on a periodic basis.

### Government Support

The Yidu government provides support to HSII. Between 2021 and 2023, the Yidu government injected assets such as mining rights, use rights of forest and equity of other local SOEs, totally valued at RMB3.5 billion, into HSII. Over the same period, the company received operational subsidies from the local government. We expect the support from the local government to remain intact given HSII's strategic importance in Yidu.

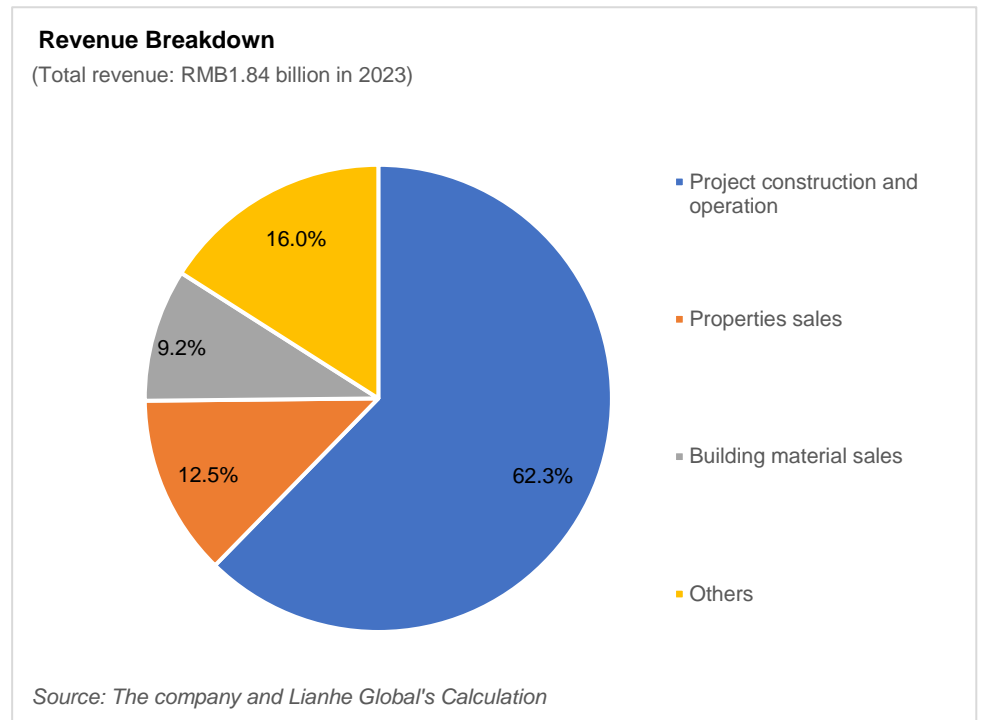
## Business Profile

### An important LIDC Responsible for project construction and industrial operation in Yidu



HSII, as an important LIDC in Yidu, is mainly responsible for project construction and industrial operation within the region, with a strong regional competitive advantage. Meanwhile, the company also engaged in diversified market businesses, such as properties sales, building materials sales, water supply, leasing business and operation services related to tourist attractions.

The company realized total revenue RMB1.84 billion, 1.87 billion, 1.84 billion and 317 million in 2021, 2022, 2023 and the first three months of 2024, respectively. The overall gross profit margin of the company was on an upward trend, increasing to 23.7% from 14.5% over the same period.



### Project Construction and Operation

HSII develops and operates industrial parks, scenic spots, water conservancy and hydropower projects, etc. in Yidu, aiming at promoting local tourism and industrial development. The company uses its own funds and borrowings to develop such projects and earns rental and operational incomes upon completion. HSII has a strong project pipeline with total planned investment amounting to c. RMB4.0 billion at end-March 2024. Yet these projects may also bring a high capital expenditure pressure on the company.

In addition, HSII undertakes projects such as pipe networking and landscaping in Yidu. The company signs construction contracts with local SOEs and settles construction costs with the entrusting parties quarterly and gets the final payment after examination of the completed projects.

### Properties Sales

HSII also engages in self-operated properties development business in Yidu by leveraging its abundant experiences in project construction. The company constructs the properties with its own funds and bank loans, and recognizes revenue upon the delivery of the

properties. The revenue derived from this segment reached RMB174 million, RMB155 million, RMB230 million and RMB5 million in 2021, 2022, 2023 and the first three months of 2024, respectively. The gross profit margin of this segment was on a downward trend, decreasing to 6.9% from 27.8% over the same period, owing to the weak property market.

### Building Material Sales and Others

HSII also sells building materials such as gravel and steel. Its other revenue was mainly derived from water supply, leasing, etc. Each of these businesses only contributed a small portion to the company's total revenue.

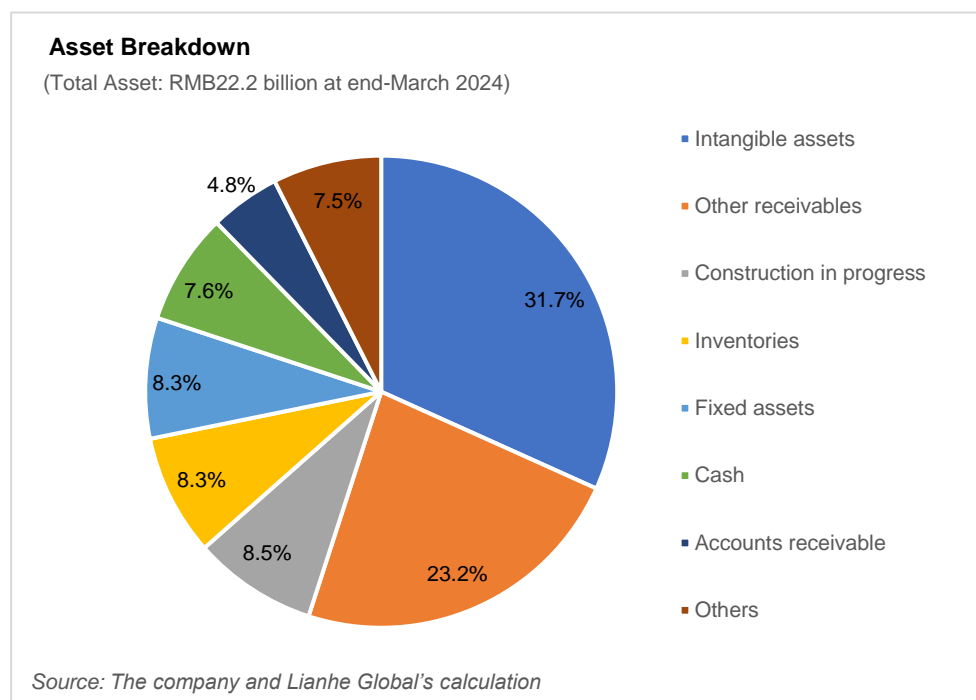
## Financial Profile

### Balance Sheet Structure and Quality

Balance Sheet Structure and Quality				
(RMB million)	2021	2022	2023	2024.3
Total Asset	17,230	19,244	21,700	22,154
Equity	9,848	9,874	12,159	12,207
Debt	4,403	5,469	5,985	6,388
Debt / (Debt + Equity) (%)	30.9	35.6	33.0	34.4
LT Debts	2,952	3,324	4,004	3,992
LT Debt / (LT Debt + Equity) (%)	23.1	25.2	24.8	24.6

*Source: HSII and Lianhe Global's calculations*

HSII's total asset increased steadily to RMB22.2 billion at end-March 2024 from RMB17.2 billion at end-2021, owing to the company's active participation in Yidu's project construction and industrial operation, as well as the asset injection. Its total debt reached RMB5.8 billion at end-March 2024, which was 62.9% higher than that at end-2021 (RMB3.6 billion). Yet its financial leverage, as measured by debt/capitalization, stayed large stable at a manageable level of 30%-35%.



HSII's asset liquidity and asset quality were relatively weak. The company had a large amount (RMB7.0 billion) of intangible assets (mainly use rights of land and water area as well as sand mining rights injected by local government), representing 31.7% of total asset at end-March 2024. At the same time, the company had sizeable other receivables and accounts receivable, totaling RMB6.2 billion and accounting for 28.1% of total asset. These receivables were concentrated with a relatively long aging. Moreover, HSII's project development activities accumulated significant inventories (mainly construction costs), construction in progress and fixed assets. These project related assets usually take a long time to monetize owing to protracted construction and payment collection periods.

### Debt Servicing Capability

The short-term debt servicing pressure of HSII was moderately high. At end-March 2024, the company had cash balance of RMB1.69 billion (including restricted cash of RMB0.95 billion), while it had debt due within one year of RMB2.40 billion. The company mainly relied on bank borrowings and other non-traditional financings to support its debt repayments and business operations. At end-March 2024, the company had unused credit line of RMB598 million.

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