

Lianhe Global has assigned ‘BBB’ global scale Long-term Issuer Credit Rating with Stable Outlook to Rizhao City Donggang District Water Group Co., Ltd.

HONG KONG, 25 October 2024 – Lianhe Ratings Global Limited (“Lianhe Global”), an international credit rating company, has assigned ‘BBB’ global scale Long-term Issuer Credit Rating to Rizhao City Donggang District Water Group Co., Ltd. (“RCDDW”). The Outlook is Stable.

The Issuer Credit Rating reflects a high possibility that the People’s Government of Donggang District, Rizhao City (“Donggang government”) would provide strong support to RCDDW if needed, in light of its indirect full ownership of RCDDW, RCDDW’s strategic importance as the key entity for developing and operating water affairs and water conservancy projects in Donggang District, Rizhao City (“Donggang”) and the linkage between the local government and RCDDW, including appointment of the senior management, strategic alignment, supervision of major investment and financing decisions and ongoing operational and financial support. In addition, the Donggang government may face significant negative impact on its reputation and financing activities if RCDDW encounters any operational and financial difficulties.

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

Key Rating Rationales

The Government’s Ownership and Supervision: The State-owned Assets Supervision and Administration Bureau of Donggang District, as the actual controller, holds 100% shares of RCDDW through Rizhao Nongfa Group Co. Ltd. The Donggang government has strong control and supervision over the company, including the appointment of senior management, decisions on its strategic development, and supervision of its major investment and funding plans. In addition, the local government has an assessment mechanism over the company and periodically appoints auditors to supervise its operating performance and financials.

Strategic Importance to Donggang and Strategic Alignment: RCDDW, as an important local investment and development company (“LIDC”) in Donggang, primarily engages in water-related affairs in the region. It is the sole entity responsible for rural water supply in the area, with a certain degree of regional advantage. It undertakes investment and construction tasks for water conservancy projects within Donggang and is also responsible for reservoir operations, rural agriculture, and rural cultural tourism activities. RCDDW plays an important role in promoting the region’s economic and social development. Its business operations and strategic planning have been aligned with the local government’s development plans.

Strong Government Support: RCDDW receives ongoing operational subsidies and asset/capital injections from the local government to support its business operations. Between

2021 and 2023, RCDDW received operational subsidies totaling RMB44.9 million from the local government. Over the same period, RCDDW received asset and equity injections in the form of water supply network assets, reservoir assets, operating rights, usage rights and other state-owned assets. We believe RCDDW will likely receive strong support from the local government in the coming years considering its strategic importance in Donggang.

Economy and Fiscal Condition of Donggang: Donggang is one of the districts under the jurisdiction of Rizhao. Its GDP growth rate has fluctuated over the past three years, with rates of 11.3%, 2.0% and 5.8% in 2021, 2022 and 2023, respectively. The GDP amount of Donggang reached RMB65.1 billion in 2023, which was ranked 1st among all jurisdiction in Rizhao.

The budgetary revenue of the Donggang government rebounded to RMB5.2 billion in 2023. It maintained a strong financial self-sufficiency with a budget surplus of 4.4% in 2023. Transfer payments from higher government have remained substantial over the past three years, amounting to RMB7.9 billion in 2023. Meanwhile, government fund income was modest at RMB29.0 million in 2023. The outstanding amount of the Donggang government's debt continued to grow between 2021 and 2023, mainly due to the rise in special debts. Its government debt ratio, as measured by total government debt outstanding/aggregate revenue, increased to 86.3% at end-2023 from 85.1% at end-2021.

RCDDW's Financial and Liquidity Position: RCDDW's total asset increased to RMB5.5 billion at end-2023 from RMB3.0 billion at end-2021, due to ongoing asset injections from the local government. The company's total debt is continuously increasing, with a high proportion of short-term debt and a high level of non-traditional financing. Its total debt increased to RMB1.8 billion at end-2023 from RMB1.2 billion at end-2021. The company's financial leverage, as measured by total liabilities/total asset, decreased from 44.3% to 40.0% over the same period driven by an increase in capital surplus.

In addition, RCDDW's asset liquidity was weak. The intangible assets made up 51.6% of the company's total assets at end-2023, primarily consisting of franchise rights and sea area usage rights. Moreover, RCDDW's short-term debt servicing pressure was moderately high. The company had a cash balance of RMB129.6 million at end-2023, compared to its short-term debts of RMB891.1 million. The company mainly relies on external financing and has access to various financing channels, including bank loans and non-traditional funding, to support its debt repayment and business operations. At end-2023, the company had unused credit facilities of RMB80.6 million.

Rating Sensitivities

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

We would consider upgrading RCDDW 's rating if (1) there is strengthened support from Donggang government, or (2) there is an upgrade in our internal credit assessment on the Donggang 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 RCDDW's rating is Lianhe Global's China Local Investment and Development Companies Criteria published on 31 July 2024, 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. None of the aforementioned entities nor its related parties participate in the credit rating process aside from providing information requested by Lianhe Global.

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