

Daye Lake High-tech Industrial Development Co., Ltd.

Initial Issuer Report

Summary

Issuer Rating	BBB
Outlook	Stable
Location	China
Industry	Local Investment and Development Companies
Date	21 January 2025

Lianhe Ratings Global Limited (“Lianhe Global”) has assigned ‘BBB’ global scale Long-term Issuer Credit Rating with Stable Outlook to Daye Lake High-tech Industrial Development Co., Ltd. (“DLHID” or “the company”)

Summary

The Issuer Credit Rating reflects a high possibility that the People’s Government of Daye City, Huangshi City (“Daye government”) would provide strong support to DLHID if needed, in light of its indirect full ownership of DLHID, DLHID’s strategic importance as the key entity for industrial park development and state-owned asset operation in Huangshi’s Daye City, Hubei Province (“Daye”), especially in Daye Lake High Tech Zone (“Daye Lake HTZ”) and the strong linkage between the Daye government and DLHID, including the control of the senior management, management supervision, strategic alignment, and ongoing operational and financial support. In addition, the Daye government may face significant negative impact on its reputation and financing activities should DLHID encounters any operational and financial difficulties.

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

Rating Rationale

The Government’s Ownership and Supervision: The Daye government indirectly holds 100% shares of DLHID through Daye Lake High-tech Industrial Investment Group Co., Ltd. (“DLHII”). The Huangshi Daye Lake High-tech Industrial Development Zone Management Committee (“Daye Lake MC”), as the representative office of the Daye government, owns 100% shares of DLHII. The Daye 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 Daye government has assessment mechanism over the company and supervises the operating performance and financial position on a periodic basis.

Strategic Importance to Daye and Strategic Alignment: DLHID, as an important local investment and development company (“LIDC”) in Daye and Daye Lake HTZ, primarily tasked with industrial parks and infrastructure development, enterprise services, and state-owned assets management. It serves as the main platform for the market-oriented transformation of state-owned enterprises in Daye and plays a crucial role in reforming local LIDCs. DLHID’s role as an operator in integrating industry and urban development within Daye Lake HTZ is increasingly prominent. Its operations and strategic planning align closely with local government development plans.

Strong Government Support: As an important part of the LIDC reform in Daye, the company benefits from favorable conditions and policies that facilitate project acquisition and resource access. The Daye government transferred equity stakes in four subsidiaries along with physical assets such as storefronts, commercial properties, and industrial parks into the company in 2022 through DLHII. This resulted in an increase of RMB3.3 billion in the company’s capital reserves in 2022. There are plans for the allocation of revenue-generating state-owned assets, such as commercial land, real estate, mineral resources,

Key Figures of Daye and DLHID

(RMB billion)

Daye	2022	2023
GDP	86.1	86.3
GDP growth rate (%)	6.5	6.2
Budgetary revenue	4.1	4.8
Government fund	8.9	3.6
Transfer payment	3.4	3.2
Budgetary expenditure	8.1	7.8
DLHID	2023	2024.6
Asset	5.6	6.5
Equity	3.6	3.6
Revenue	0.58	0.43

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

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Applicable Criteria

China Local Investment and Development Companies Criteria
 (31 July 2024)

and rights-of-use assets, to expand the company's total assets and enhance its operational capabilities and future growth. Additionally, the government provides ongoing financial support to strengthen the company's capital capabilities.

Economy and Fiscal Condition of Daye: Daye is a county-level city of Hubei Province ("Hubei") and is managed by Huangshi City ("Huangshi"). It ranks 49th among the top 100 counties and cities in China in terms of comprehensive strength. Daye maintained medium-high economic growth during the past three years, with its GDP growth rate recording 14.4%, 6.5% and 6.2% in 2021, 2022 and 2023, respectively. The GDP amount of Daye reached RMB86.3 billion in 2023, which was ranked 1st among all Huangshi's jurisdictions. Daye Lake HTZ is a national high-tech industrial development zone. It has a total land area of 7.4 square kilometers. It focuses on innovation-driven development and optimizing the innovation ecosystem to enhance autonomous innovation, cultivate new industries, and boost traditional industries.

The budgetary revenue of the Daye government increased to RMB4.8 billion in 2023 from RMB4.1 billion in 2021, while the contribution of tax revenue was down to 73.0% from 74.8% over the same period. The financial self-sufficiency of Daye was weak but improving, with the budget deficit narrowing to 63.9% in 2023 from 95.2% in 2021. The government fund income plummeted to RMB3.6 billion in 2023 from RMB5.6 billion in 2021, due to the downturn of the real estate industry. Its fiscal debt ratio, as measured by total government debt outstanding/aggregate revenue, surged to 120.8% at end-2023 from 66.9% at end-2021.

DLHID's Financial and Liquidity Position: In 2023, the company's operating income experienced significant growth. From the perspective of revenue composition, the sales income from recycled aluminum and real estate sales are vital components of the company's operating income. The revenue from recycled aluminum sales has seen a substantial increase due to the expansion of the subsidiary's business scale. DLHID's total assets rose to RMB6.5 billion at end-June 2024 from RMB5.0 billion at end-2022 due to asset injections from the local government. The company's total debt increased to RMB1.4 billion at end-June 2024 from RMB309.5 million at end-2022, with a high proportion of short-term debt (66.8% at end-June 2024). The company's financial leverage, as measured by total liabilities/total asset, increased from 30.5% to 45.2% over the same period.

DLHID's asset liquidity was moderate. Investment properties made up 34.5% of the company's total assets at end-June 2024, primarily consisting of storefront and commercial properties injected from DLHII. Besides, DLHID's short-term debt servicing pressure was moderately high. 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.

Rating Sensitivities

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

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

Operating Environment

Daye is a county-level city of Hubei and is managed by Huangshi. Daye is one of the top 100 industrial counties in China and ranked 49th in the list of Top 100 Counties in China in 2023, indicating advanced industrial capacity and profitability. Daye has jurisdiction over 10 towns, 4 communities, 1 national high-tech zone and 1 state-owned farm, with a total land area of 1,566 square kilometers. At end-2023, Daye had a residential population of 0.9 million, with an urbanization rate of 63.4%.

Daye maintained medium-high economic growth during the past three years, with its GDP growth rate recording 14.4%, 6.5% and 6.2% in 2021, 2022 and 2023, respectively. The GDP amount of Daye reached RMB86.3 billion in 2023, which was ranked 1st among all Huangshi's jurisdictions. The economic structure of Daye was mainly driven by the secondary and tertiary industries, which accounted for 53.1% and 39.9% of its GDP in 2023, respectively.

Daye Lake HTZ is located in the middle of Daye. It has a total land area of 7.4 square kilometers. It focuses on innovation-driven development and optimizing the innovation ecosystem to enhance autonomous innovation, cultivate new industries, and boost traditional industries, positioning itself as a key driver for regional economic transformation and a leader in high-tech industries.

Daye's GDP and Fixed Asset Investment

(RMB billion)	2021	2022	2023
GDP	75.1	86.1	86.3
-Primary industry (%)	7.3	6.8	7.0
-Secondary industry (%)	55.5	57.7	53.1
-Tertiary industry (%)	37.3	35.5	39.9
GDP growth rate (%)	14.4	6.5	6.2
Fixed asset investment	59.5	71.1	75.1
Fixed asset investment growth rate (%)	30.7	19.5	5.6
Population (million)	0.9	0.9	0.9

Source: Public information and Lianhe Global's calculations

Fiscal Condition of Daye

The aggregate fiscal revenue of the Daye government was mainly derived from budgetary revenue and government fund income. The budgetary revenue of the Daye government increased to RMB4.8 billion in 2023 from RMB4.1 billion in 2021, while the contribution of tax revenue was down to 73.0% from 74.8% over the same period. The financial self-sufficiency of Daye was weak but improving, with the budget deficit narrowing to 63.9% in 2023 from 95.2% in 2021. The government fund income plummeted to RMB3.6 billion in 2023 from RMB5.6 billion in 2021, due to the downturn of the real estate industry.

The outstanding amount of the Daye government's debt continued to grow in 2021-2023, mainly due to the rise in special debts. By the end of 2023, the Daye government's outstanding debt was RMB14.0 billion, including RMB5.7 billion of general obligations and RMB8.3 billion of special debts. Its fiscal debt ratio, as measured by total government debt outstanding/aggregate revenue, surged to 120.8% at end-2023 from 66.9% at end-2021.

Daye's Fiscal Conditions			
(RMB billion)	2021	2022	2023
Budgetary revenue	4.1	4.1	4.8
Budgetary revenue growth rate (%)	50.2	9.1*	16.6
Tax revenue	3.0	3.1	3.5
Tax revenue (% of budgetary revenue)	74.8	75.3	73.0
Government fund income	5.6	8.9	3.6
Transfer payment	2.7	3.4	3.2
Aggregate revenue	12.4	16.4	11.6
Budgetary expenditure	7.9	8.1	7.8
Budget deficit ¹ (%)	-95.2	-98.1	-63.9

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

Source: Public information and Lianhe Global's calculations

Ownership Structure

Government's Ownership

DLHID was established in 2016. After a series of capital replenishments and equity transfers, the company's paid-in capital was enlarged to RMB80.0 million at end-June 2024. The Daye Lake MC, as the actual controller, holds the full shares of DLHID through DLHII.

Strategic Importance and Government Linkage

Strategic Importance of DLHID to Daye

DLHID, as an important LIDC in Daye and Daye Lake HTZ, primarily tasked with industrial parks and infrastructure development, enterprise services, and state-owned assets management. It serves as the main platform for the market-oriented transformation of state-owned enterprises in Daye and plays a crucial role in reforming local LIDCs. DLHID's role as an operator in integrating industry and urban development within Daye Lake HTZ is increasingly prominent. Its operations and strategic planning align closely with local government development plans.

Strong Linkage with the Local Government

DLHID's linkage with the Daye government is strong. The local government indirectly holds the full ownership of DLHID and is the company's actual controller. The local 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.

Strong Government Support

As an important part of the LIDC reform in Daye, the company benefits from favorable conditions and policies that facilitate project acquisition and resource access. The Daye government transferred equity stakes in four subsidiaries along with physical assets such as storefronts, commercial properties, and industrial parks into the company in 2022 through DLHII. This resulted in an increase of RMB3.3 billion in the company's capital reserves in 2022. There are plans for the allocation of revenue-generating state-owned assets, such as commercial land, real estate, mineral resources, and rights-of-use assets, to expand the company's total assets and enhance its operational capabilities and future growth.

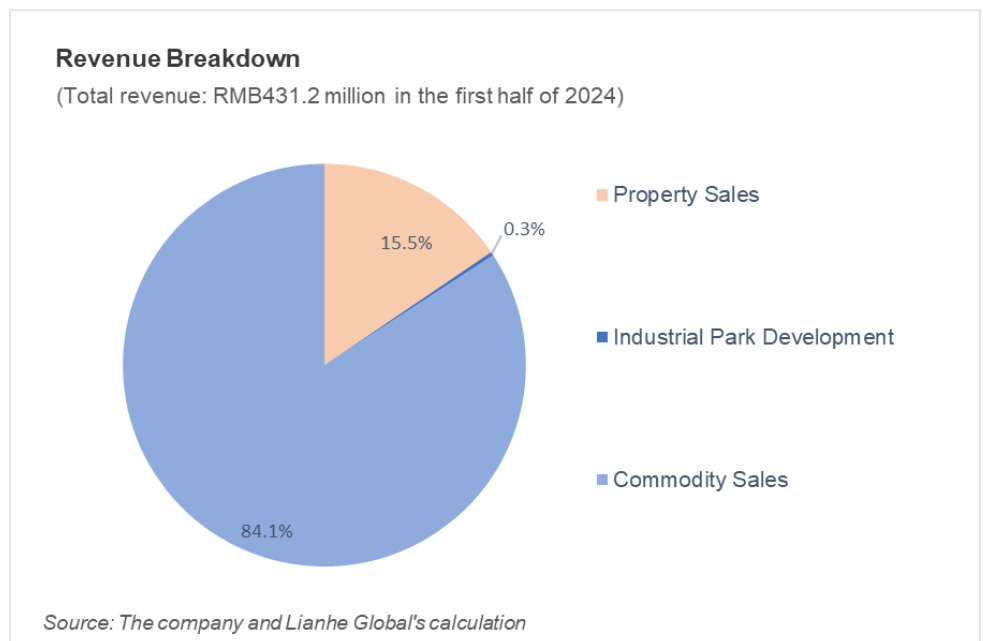
Additionally, the government provides ongoing financial support to strengthen the company's capital capabilities.

Business Profile

An important LIDC Responsible for Industrial Park Development and Infrastructure Construction in Daye Lake HTZ

DLHID, as an important LIDC in the Daye, is responsible for industrial park development and state-owned assets operation within the region, with a strong regional advantage. In addition, the company has received strong support from the government in terms of capital injection and asset transfer, which enhances the capital strength and profitability of the company.

DLHID's operating revenue sources are industrial park development, commodity sales and property sales business. The company's total revenue had an upward trend, recording at RMB2.7 million, RMB36.5 million, RMB582.6 million and RMB431.2 million in 2021, 2022, 2023 and the first six months of 2024, respectively. The overall gross profit margin of DLHID fluctuated between 3.9% and 14.1% over the same period. In general, DLHID's business was relatively concentrated, and it has regional advantages in its major businesses.



Industrial Park Development

DLHID is responsible for the investment, construction, and subsequent operation of major industrial parks within the Daye Lake HTZ. The main assets under operation include the Electronic Information Industrial Park, along with commercial and storefront properties at end-June 2024. The business model involves signing lease agreements with companies in the industrial parks, renting out buildings and factories, and charging rental and property management fees based on the rented area.

The revenue from this segment was RMB2.5 million, RMB2.0 million, RMB1.8 million and RMB1.5 million in 2021, 2022, 2023 and the first six months of 2024. The gross profit margin remained relatively high at 84%-92% in the corresponding periods. The Electronic

Information Industrial Park has not yet generated rental income at end-June 2024, as the tenant companies, attracted through investment promotion, are currently in a rent-free period. The segment is expected to generate more income in the future.

Commodity Sales

The commodity sales business of the company began at end-2022, primarily focusing on scrap aluminium. It aims to support the development of over 30 aluminium-related industries within the industrial park in Daye Lake HTZ. The company sets purchase and supply prices according to market principles, achieving diversified revenue.

The revenue generated from this segment reached RMB16.8 million, RMB300.0 million and RMB362.7 million in 2022, 2023 and the first six months of 2024, representing an upward trend. Since its inception, the gross profit margin of this segment has remained relatively low, staying below 1% over the past few years.

Property Sales

DLHID's property sales business mainly focused on residential properties. It invested its own land to jointly establish a project company with private real estate developers to develop real estate projects. Once the projects are completed, the project company is responsible for external sales. The company did not recognize any residential property sales revenue in 2021. It recognized sales revenue of RMB17.8 million, RMB280.9 million and RMB67.0 million in 2022, 2023 and the first six months of 2024, respectively. There are no planned residential projects in the pipeline as of end-June 2024.

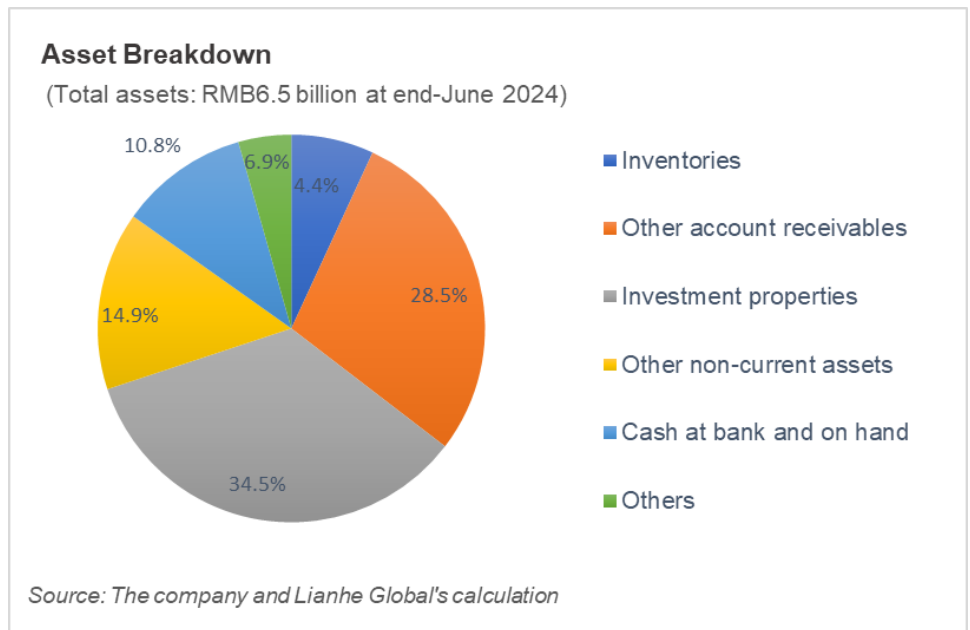
Financial Profile

Balance Sheet Structure and Quality

Balance Sheet Structure and Quality				
(RMB million)	2021	2022	2023	2024.6
Total Asset	4,612	4,989	5,625	6,496
Equity	3,493	3,467	3,585	3,559
Debt	51	310	517	1,401
Debt / (Debt + Equity) (%)	1.4	8.2	12.6	28.3
LT Debts	0	165	68	465
LT Debt / (LT Debt + Equity) (%)	-	4.6	1.9	11.6

Source: DLHID and Lianhe Global's calculations

DLHID's total assets rose to RMB6.5 billion at end-June 2024 from RMB5.0 billion at end-2022 due to asset injections from DLHII and the Daye government. The company's total debt increased to RMB1.4 billion at end-June 2024 from RMB309.5 million at end-2022, with a high proportion of short-term debt (66.8% at end-June 2024). The company's financial leverage, as measured by total liabilities/total asset, increased from 30.5% to 45.2% over the same period, but remained at a relatively low level. The company's debt is primarily composed of bank loans, with a small proportion of non-standard financing, which is not expected to increase.



DLHID's asset liquidity was weak. Investment properties made up 34.5% of the company's total assets at end-June 2024, primarily consisting of storefront and commercial properties injected from DLHII. Additionally, the company's project development activities accumulated sizeable inventories (mainly construction costs) and receivables (mainly due from government agencies and other LIDCs), accounting for 32.9% of the total asset at end-June 2024. These assets usually take a long time to monetize due to the protracted construction and payment collection period.

Debt Servicing Capability

DLHID's short-term debt servicing pressure was moderate. The company had a cash balance of RMB700.0 million at end-June 2024, compared to its short-term debts of RMB935.9 million. The company's borrowings primarily consist of short-term bank loans, most of which can be renewed. 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.

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