CCXAP assigns first-time long-term credit rating of BBB_g+ to Shaoxing Shangyu State-owned Capital Investment and Operation Co., Ltd., with stable outlook.

Hong Kong, 3 November 2022 – China Chengxin (Asia Pacific) Credit Ratings Company Limited ("CCXAP") has assigned a first-time long-term credit rating of BBB_g+ to Shaoxing Shangyu State-owned Capital Investment and Operation Co., Ltd. ("SYSC" or the "Company"), with stable outlook.

The BBBg+ long-term credit rating of SYSC reflects (1) Shangyu District Government's strong capacity to provide support; and (2) the local government's extremely high willingness to provide support, based on our assessment of the Company's characteristics. Our assessment of Shangyu District Government's capacity to provide support reflects the Shangyu District's relatively good comprehensive strength, with fast economic growth and good fiscal balance.

The rating also reflects the local government's willingness to provide support, which is based on the Company's (1) full and direct ownership by the local government; (2) important policy role in Shangyu District as the largest state-owned enterprise ("SOE"); (3) good access to funding; and (4) good track record of receiving government payments. However, the rating is constrained by the Company's (1) moderate exposure to commercial business activities; (2) moderate debt management and weak asset liquidity; and (3) moderate exposure to contingent liabilities.

Corporate Profile

Established in 1994, SYSC is the largest local infrastructure investment and financing company ("LIIFC") in Shangyu District, Shaoxing City in terms of total assets. As the main operator and developer in Shangyu District, the Company engages in diversified businesses, including water supply and wastewater treatment, land development, construction, resettlement housing, municipality operation, and commodity transaction businesses.

In September 2021, the local Government transferred 100% equity interest of Shaoxing Shangyu Economic Development Zone Investment Development Group Co., Ltd. and 18% of Shaoxing Shangyu Hangzhou Bay Construction and Development Co., Ltd. from the Company to Shaoxing Shangyu Hangzhou Bay Economic Zone Holdings Co., Ltd. ("Shangyu Hangzhou Bay Holdings"), and transferred 51% equity interest in Shaoxing Shangyu District Transportation Group Co., Ltd. ("Transportation Group") and 20% equity interest in Shaoxing Shangyu Hangzhou Bay Holdings to the Company. As of 30 June 2022, the Company was wholly owned and directly controlled by State-owned Assets Supervision and Administration Commission of Shaoxing City Shangyu District ("Shangyu SASAC").

Rating Rationale

Credit Strengths

Important policy role in Shangyu District as the largest SOE. SYSC is the largest LIIFC in terms of total assets in Shangyu District and the primary LIIFC wholly owned and effectively controlled by the Shangyu District Government to participate in the operation and development of Shangyu District. Positioned as the main developer in Shangyu District, SYSC undertakes various public-related activities such as water supply and wastewater treatment, land development, infrastructure construction, resettlement housing and grain storage, which significantly benefits people's livelihood and promotes the process of urbanization.

Good access to fundings. SYSC has sufficient stand-by liquidity and diversified funding channels. As of 30 June 2022, the Company's total credit facilities amounted to RMB47.5 billion, of which the unutilized portion was RMB11.4 billion. The Company has a proven track record of financing from both onshore and offshore debt markets. For example, during the first ten months of 2022, the Company itself raised RMB6.0 billion through the onshore debt market with coupon rates ranged from 3.07% to 3.49% and raised USD300 million with a coupon rate of 5.2% through the offshore debt market.

Good track record of receiving government payments. SYSC has a good track record of receiving payments from the local government in terms of capital injections, asset injections, financial subsidies, infrastructure and land development repayments. From 2020 to 2022H1, the local government totally injected cash and assets such as equity shares and use right of land of RMB32.2 billion into the Company, significantly enhancing its capital strength. Furthermore, the local government consistently provides subsidies to the Company to support its operation, with a total amount of RMB3.9 billion from 2020 to 2022H1.

Credit Challenges

Moderate exposure to commercial business activities. SYSC also engages in commercial business activities, including commodity transaction, sales of transportation infrastructure materials and refined oil, engineering construction and municipality operation, which generate supplementary revenue and profit to the Company. We estimate that SYSC had moderate commercial exposure, with the assets of commercial businesses accounting for 15% to 20% of its total assets.

Moderate debt management and asset liquidity. SYSC's total debt increased moderately in the past three years, with high portion of short-term debt. The Company's total debt increased from RMB55.7 billion at end-2019 to RMB88.5 billion at mid-2022, with total capitalization ratio of 54.5% and short-term debt accounting for 38.7%. In addition, the liquidity profile was weak with cash to short-term debt ratio of 0.5x at mid-2022, indicating that its cash balance was insufficient to cover its short-term debt. SYSC's asset liquidity is relatively weak as its assets are mainly illiquid inventories and non-current assets.

Moderate exposure to contingent liabilities. SYSC had moderate exposure to contingent liabilities as its external guarantees were 25.6% relative to total equity as of 30 June 2022. The external guarantees amounted to RMB19.7 billion, all of which were provided to bank borrowings or bond issuance from state-owned enterprises in Shangyu District and Zhejiang Province. In case a credit event occurs, the Company may face certain contingent liability risks and cross default risks, which could negatively impact its credit quality.

Rating Outlook

The stable outlook on SYSC's rating reflects our expectation that Shangyu District Government's capacity to provide support will remain stable, and the Company will maintain its vital position in Shangyu District.

What could upgrade the rating?

The rating could be upgraded if (1) Shangyu District Government's capacity to support strengthens; and (2) the Company's characteristics change in a way that strengthens the local government's willingness to support, such as a substantial reduction in external guarantees or improved debt management.

What could downgrade the rating?

The rating could be downgraded if (1) Shangyu District Government's capacity to support weakens; or (2) the Company's characteristics change in a way that weakens the local government's willingness to support, such as a reduction in importance of its policy role, a substantial reduction in government payments, or deteriorated debt management.

Rating Methodology

The methodology used in this rating is the Rating Methodology for China's Local Infrastructure Investment and Financing Companies (July 2022).

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