

Credit Opinion

14 April 2025

Ratings	
Category	Corporate
Domicile	China
Rating Type	Solicited Rating
Long-term Credit Rating	BBB _g -
Outlook	Stable

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Shandong Luzhong Investment Co., Ltd.

Surveillance credit rating report

CCXAP affirms Shandong Luzhong Investment Co., Ltd's long term credit rating at BBB_g-, with stable outlook.

Summary

The BBB_g- long-term credit rating of Shandong Luzhong Investment Co., Ltd. ("SDLZ" or the "Company") reflects Yiyuan County Government's relatively strong capacity to provide support and its very extremely high willingness to provide support based on our assessment of the Company's characteristics.

Our assessment of Yiyuan County Government's capacity to support reflects its location advantage in Zibo City with steady economic growth, but constrained by its modest fiscal profile.

The rating also reflects the local government's willingness to support, which is based on the Company's (1) important role in local economic development and infrastructure construction in Yiyuan County; and (2) good track record of receiving government payments.

However, the rating is constrained by the Company's (1) increasing exposure to commercial activities; (2) rising investment needs that will heighten its debt leverage; and (3) moderate funding access.

The stable outlook on SDLZ's rating reflects our expectation that the Yiyuan County Government's capacity to provide support will remain stable, and the Company will maintain its importance in the development of Yiyuan County over the next 12 to 18 months.

Rating Drivers

- Important role in local economic development and infrastructure construction in Yiyuan County
- Good track record of receiving government payments
- Increasing exposure to commercial activities
- Increasing debt burden with short-term debt pressure
- Moderate access to funding channels
- Medium exposure to contingent liabilities

Rating Sensitivities

What could upgrade the rating?

The rating could be upgraded if (1) Yiyuan County Government's capacity to provide support strengthens; and (2) the Company's characteristics change in a way that strengthens the local government's willingness to provide support, such as improved refinancing ability.

What could downgrade the rating?

The rating could be downgraded if (1) Yiyuan County Government's capacity to provide support weakens; or (2) the Company's characteristics change in a way that weakens the local government's willingness to provide support, such as reduced strategic significance, or deteriorated debt management.

Key Indicators

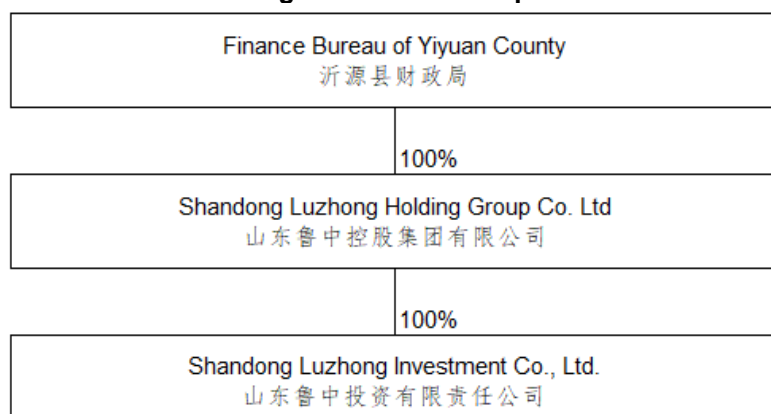
	2021FY	2022FY	2023FY	2024Q3
Total Asset (RMB billion)	9.0	11.9	12.5	16.0
Total Equity (RMB billion)	5.1	7.4	7.9	8.1
Total Revenue (RMB billion)	4.1	4.5	5.4	3.8
Total Debt/Total Capital (%)	32.3	28.7	30.0	43.6

All ratios and figures are calculated using CCXAP's adjustments.

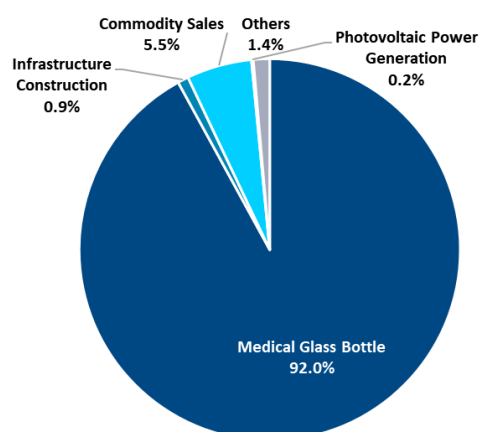
Source: Company data, CCXAP research

Corporate Profile

Founded in 2016, SDLZ is one of the major local state-owned enterprises that is responsible for local investment and infrastructure construction in Yiyuan County. The Company also diversified into other commercial business, including medical glass bottle sales, self-operated construction, commodity sales, and photovoltaic power generation business. SDLZ is the largest shareholder of Shandong Pharmaceutical Glass Co., Ltd ("SDPG") (Stock Code: 600529.SH), which is a leading pharmaceutical glass packaging manufacturer in China and headquarter in Yiyuan County. As of 30 September 2024, the Company is owned and controlled by the Finance Bureau of Yiyuan County ("Yiyuan Finance Bureau") through Shandong Luzhong Holding Group Co., Ltd.

Exhibit 1. Shareholding chart as of 30 September 2024

Source: Company information, CCXAP research

Exhibit 2. Revenue structure in 2023

Source: Company information, CCXAP research

Rating Considerations**Government's Capacity to Provide Support**

We believe Yiyuan County Government has a relatively strong capacity to provide support given its good economic fundamentals and fiscal strengths.

Shandong Province is the third largest province in terms of gross regional product ("GRP") in China over the past three years, with a solid industrial foundation in logistics, shipbuilding and marine technology, chemical, automotive and agri-food. Zibo City is located in the central part of Shandong Province, which is one of the core cities of Shandong Peninsula Urban Agglomeration and a regional central city in Shandong Province approved by the State Council. Zibo City reported a GRP of RMB488.4 billion in 2024, ranking the 7th by GRP among 16 prefecture-level cities in Shandong Province over the past three years. Zibo City has relatively strong fiscal strength and a manageable debt profile. In 2024, its general budgetary revenue covered around 70% of its general budgetary expenditure, and tax incomes accounted for nearly 55% of its general budgetary revenue. As of end-2024, Zibo City's government debt balance was RMB142.7 billion, accounting for 29.2% of GRP.

Exhibit 3. Key economic and fiscal Indicators of Zibo City

	2022FY	2023FY	2024FY
GRP (RMB billion)	440.3	456.2	488.4
GRP Growth (%)	4.7	5.5	5.5
General Budgetary Revenue (RMB billion)	37.6	39.5	41.1
General Budgetary Expenditure (RMB billion)	52.6	55.0	57.8
Local Government Debt (RMB billion)	108.0	122.6	142.7

Source: Statistics Bureau of Zibo City, CCXAP research

Yiyuan County is a county-level city under the jurisdiction of Zibo City, and is located in the middle of Shandong Province, with a total area of 1,636 square kilometers. With years of development, Yiyuan County has formed three core industries, including new medicine, new materials, electronic information industries; more than 100 large enterprises have settled in Yiyuan County. It has demonstrated stable economic growth in recent years. In 2024, the GRP of Yiyuan County increased to RMB36.6 billion, representing a YoY increase of 7.0%. Yiyuan County had a modest financial profile. It reported a general public budget revenue of RMB2.5 billion in 2024. The tax revenues have been increasing over the past two years, reaching RMB1.6 billion in 2024, accounting for 64.9% of the general budgetary revenue. In addition, Yiyuan County has a relatively weak self-sufficiency, with fiscal balance ratios (general budgetary revenue/general budgetary expenditure) around 50% over the past three years. As of end-2024, Yiyuan County's government debt balance was RMB9.3 billion, accounting for 25.4% of GRP.

Exhibit 4. Key economic and fiscal indicators of Yiyuan County

	2022FY	2023FY	2024FY
GRP (RMB billion)	32.9	34.3	36.6
GRP Growth (%)	7.3	6.0	7.0
General Budgetary Revenue (RMB billion)	2.2	2.4	2.5
General Budgetary Expenditure (RMB billion)	4.4	4.7	4.7
Local Government Debt (RMB billion)	5.9	7.3	9.3

Source: Statistics Bureau of Yiyuan County, CCXAP research

Government's Willingness to Provide Support**Important role in local infrastructure construction in Yiyuan County**

SDLZ is one of the major local state-owned enterprises in Yiyuan County and undertakes local infrastructure construction and industrial investments in Yiyuan County. SDLZ's infrastructure projects are crucial to local social and economic development that benefits the general public and local employment. We believe that the Company will maintain an important position in the public policy projects in Yiyuan County and will not be easily replaced by other local state-owned enterprises in the foreseeable future.

The Company undertakes infrastructure construction through agency construction model. SDLZ signed construction agreements with Yiyuan Finance Bureau and will receive payments based on the total cost plus a certain markup in return during the construction progress or after the project is completed. As of 30 September 2024, the Company had 2 projects under construction, including the construction of chemical park infrastructure and rural improvement, with total investment of around RMB1.2 billion and uninvested amount of RMB678.0 million. The Company had no planned infrastructure construction project and is expected to take more construction project under self-construction mode in the future.

Increasing exposure to commercial business activities

SDLZ participates in different commercial activities, including medical glass bottle sales and commodity sales business. While the commercial activities generate supplemental income, they may also pose higher operational and business risks than its public-policy businesses. We consider that the Company's risk exposure to commercial activities is low but rising as SDLZ increasing its investment in self-operated projects.

SDLZ's listed subsidiary, SDPG (Stock Code: 600529.SH), is responsible for the medical glass bottles sales business. SDPG engages in the research, development, production and sales of various medicinal glass bottle products. SDPG has six major products, which are used in the packaging of various types of medicines, health products, and cosmetics products. SDPG mainly adopts demand-on-production mode for the medical glass bottles sales business, and the products are sold to large domestic and overseas customers, such as Qilu Pharmaceutical Co., Ltd., Yangze River Pharmaceutical (Group) Co., Ltd., and Bayer Healthcare Limited. The revenue from the medical glass bottles sales business increased from RMB4.1 billion in 2022 to RMB4.9 billion in 2023, which has contributed considerable amount of income to the Company. The net income of SDPG was RMB775.8 million in 2023, increasing from RMB618.3 million in 2022, representing a 25.5% YoY increase. The decline in its net profit margin stems mainly from the rising cost of raw materials, such as borax and soda ash. SDPG's sales revenue was recorded at RMB2.6 billion for the first half of 2024, representing a YoY increase of 6.8%. Furthermore, SDPG's asset-liability ratio was relatively low at 24.8% as of 30 June 2024. Overall, SDPG has demonstrated stable operations and relatively good profitability over the past three years. Meanwhile, the Company receives share dividends from SDPG every year. In 2022 and 2023, it had received a total of RMB38.8 in dividends from SDPG respectively. As of 30 September 2024, SDPG had 4 key projects under construction, with a total investment of RMB2.8 billion, which are expected to further increase the Company's production capability in the future.

SDLZ also had some self-operated construction projects. As of 30 September 2024, the Company had 2 projects under construction, including digital intelligence logistics infrastructure and talent apartment. Meanwhile, the Company had 2 construction projects under planning, with a total investment of RMB1.4 billion. The Company is expected to achieve fund balancing through future operating income, such as leasing income, and sales of agricultural product. However, the investment recovery cycle is long, making it more difficult to achieve fund balancing in short period of time. Furthermore, the relatively large scale of investment will bring more pressure on the capital expenditure of the Company.

SDLZ also engages in commodity sales business, the main product is ethylene. The Company only sell the products to downstream customers when receiving full payment. However, the concentration risk from upstream and downstream customers are high, with only one upstream supplier and one downstream customer, which are state-owned enterprises in Yiyuan County. Moreover, the gross profit of this business sector generated by the Company is low. There is an uncertainty in the future earnings of the Company's commodity sales business.

Good track record of receiving government payments

SDLZ has a proven track record of receiving support from the local government in terms of capital injections, project payment, and subsidies. In 2019, the local government transferred its shareholdings of a listed company to the Company, namely SDPG, diversifying the business scope of the Company. SDLZ also has a good track record of receiving government payments. From 2023 to 2024Q3, SDLZ continuously received government subsidies with a total amount of around RMB44.5 million, including fiscal and operating subsidies, which support its future investments and debt repayments. As of 30 September 2024, SDLZ has received total project repayments of about RMB100 million from the local government for its infrastructure construction projects. We

expect that, as the key local state-owned enterprise in Yiyuan County, the Company plays an irreplaceable role in the development and operation of the region, and will continue to receive government support over the next 12 to 18 months.

Increasing debt burden with short-term debt pressure

Due to the continuous investment in infrastructure construction projects, SDLZ's total debt has been growing over the past three years. As of 30 September 2024, the Company's total debt increased to RMB6.2 billion from RMB3.0 billion as of end-2022. The Company has maintained moderate debt leverage. Its total capitalization ratio, as measured by total debt to total capital, was recorded at 43.6% as of the same date. However, the Company is exposed to certain short-term debt repayment pressure. As of 30 September 2024, its short-term debt was RMB1.9 billion, accounting for around 30.9% of total debt. Meanwhile, after excluding restricted cash, the cash to short-term debt ratio was 0.5x, which could not fully cover the short-term debt. Given the Company's future capital expenditure pressure for its investment and construction projects, we expect the Company's debt level will continue to increase for the next 12-18 months.

Moderate funding access

SDLZ had access to various sources of funding, including bank loans, onshore and offshore bond financing and non-standard financing. The Company maintains long-term relationships with several banks, such as Agricultural Development Bank of China and China Bohai Bank Co., Ltd. However, the funding sources of the Company were mainly from regional banks in Shandong Province. As of 30 September 2024, the Company had total bank credit facilities of RMB2.4 billion, with an unutilized portion of RMB1.3 billion. Moreover, the Company's financing also relies on stock pledged loans and loans obtained through guarantees from other state-owned enterprises. As of 29 March 2025, the Company had pledged about 45% of its shares in its subsidiary SDPG, receiving a total of around RMB750 million in financing, with limited room of further pledging.

The Company also has a good track record for fund-raising activities in capital market. In 2024, the Company issued 4 tranches of onshore private placement notes, raising RMB2.1 billion. It also has an access to offshore bond market. As of 30 September 2024, the Company's exposure to non-standard financing accounted for 10%-15% of the total debts. As these types of financing generally have high financing cost and short-term borrowing period, which may enlarge SDLZ' refinancing pressure.

Medium exposure to contingent risk

The Company bears moderate contingent risk resulting from relatively large external guarantees, which could potentially increase its repayment obligations. As of 30 September 2024, the Company's external guarantees amounted to RMB2.4 billion, accounting for 29.2% of its net assets. Most of the external guarantees were provided to state-owned enterprises in Yiyuan County. Considering the government's support for local state-owned enterprises, we believe the credit risk of the guarantee is controllable.

ESG Considerations

SDLZ assumes environmental risks through its infrastructure construction projects. Such risks could be moderated through environmental studies and detailed planning prior to the start of the projects and close supervision during construction.

SDLZ bears social risks as it implements public policy initiatives by building public infrastructure in Yiyuan County. Demographic changes, public awareness and social priorities shape the Company's development targets and ultimately affect the local government's propensity to support the Company.

SDLZ's governance considerations are also material as the Company is subject to oversight by Linyi County Government and has to meet several reporting requirements, reflecting its public-policy role and status as a government-owned entity.

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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