

Credit Opinion

16 May 2023

Ratings	
Senior Unsecured Debt Rating	BBB _g -
Long-Term Credit Rating	BBB _g -
Outlook	Stable
Category	Corporate
Domicile	China
Rating Type	Solicited Rating

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Dujiangyan Smart City Operation and Construction Development Group Co., Ltd.

Initial credit rating report

CCXAP assigns first-time long-term credit rating of BBB_g- to Dujiangyan Smart City Operation and Construction Development Group Co., Ltd., with stable outlook.

Summary

The BBB_g- long-term credit rating of Dujiangyan Smart City Operation and Construction Development Group Co., Ltd. (“DSOC” or the “Company”) reflects Dujiangyan City Government’s relatively strong capacity and extremely high willingness to provide support to the Company, based on our assessment of the Company’s characteristics.

Our assessment of the Dujiangyan City Government’s capacity to provide support reflects Dujiangyan City’s vital position in Chengdu City, given its good cultural and tourism resources, but relatively weak industrial base.

The rating also reflects the local government’s willingness to provide support, which is based on the Company’s (1) important role as the major infrastructure constructor and urban operator in Dujiangyan City; and (2) solid track record of receiving government payments.

However, the rating is constrained by the Company’s (1) relatively high reliance on non-standard financing; (2) medium exposure to contingent risk; and (3) moderate assets liquidity.

The stable outlook on DSOC’s rating reflects our expectation that the local government’s capacity to support the Company will remain stable, and the Company will maintain its important position in the infrastructure construction and urban operation in Dujiangyan City.

Rating Drivers

- Important role as the major infrastructure constructor and urban operator in Dujiangyan City
- Solid track record of receiving government payments
- Increasing debt burden and moderate asset liquidity
- Relatively high reliance on non-standard financing
- Medium exposure to contingent risk

Rating Sensitivities

What could upgrade the rating?

The rating could be upgraded if (1) the local government's capacity to provide support strengthens; and (2) changes in company's characteristics enhance local government's willingness to provide support, such as decreased exposure to contingent risk and increased asset liquidity.

What could downgrade the rating?

The rating could be downgraded if (1) the local government's capacity to provide support weakens; or (2) changes in company characteristics decrease the local government's willingness to provide support, such as reduced regional significance.

Key Indicators

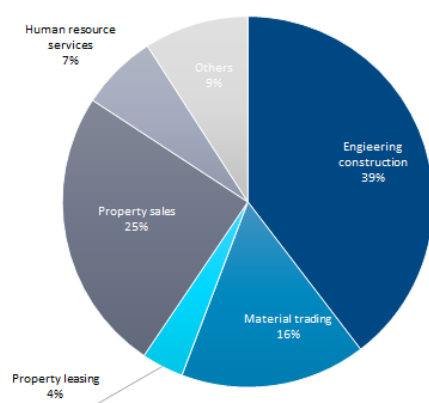
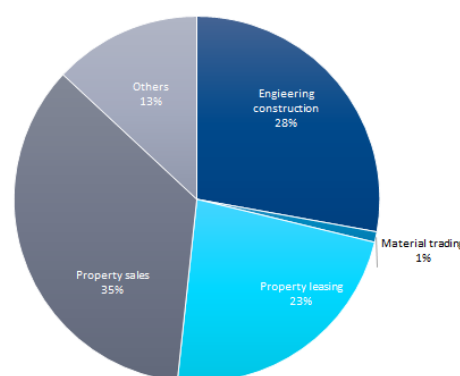
	2020FY	2021FY	2022FY
Total Asset (RMB billion)	25.1	26.8	27.7
Total Equity (RMB billion)	11.0	11.3	11.4
Total Revenue (RMB billion)	0.9	0.9	1.1
Total Debt/Total Capital (%)	34.1	35.7	41.1

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

Source: CCXAP research

Corporate Profile

Founded in 2016, formerly known as Dujiangyan Xincheng Equity Investment Co., Ltd., DSOC is one of the 5 key subsidiaries of Chengdu Dujiangyan Investment Development Group Co., Ltd. ("CDID"). The Company is primarily responsible for infrastructure construction and resettlement housing construction in Dujiangyan City. Apart from public development projects, DSOC has a clear positioning of urban operation. The Company also derives revenue from businesses such as property sales, material trading, property leasing and management, carparking services and human resource services. As of 31 December 2022, CDID held 90% and Sichuan Provincial Department of Finance held the remaining 10% of the Company's shares. The Company was ultimately controlled by Dujiangyan State-owned Assets Supervision and Administration and Finance Bureau ("Dujiangyan SASAFB").

Exhibit 1. Revenue Structure in 2022**Exhibit 2. Gross profit Structure in 2022**

Source: Company information, CCXAP research

Exhibit 3. Shareholding chart as of 31 December 2022

Source: Company information, CCXAP research

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

We believe the Dujiangyan City Government has a relatively strong capacity to provide support to the Company, given its good cultural and tourism resources, but relatively weak industrial base.

Sichuan Province is a leading economic province and is recognized as one of the most developed provinces in China. In 2022, Sichuan recorded a gross regional product ("GRP") of RMB5.6 trillion, with a GRP growth rate of 2.9% year on year ("YoY"), ranking 6th in terms of GRP among all provinces in China. Its general budgetary revenue increased to RMB488.2 billion, up 2.3% YoY.

Chengdu City is a sub-provincial city that serves as the capital city of Sichuan Province. Chengdu City is also an important economic and financial center, as well as a transportation and communication hub in Southwest China, with a solid economic foundation. Its economy is characterized by industries such as electronic information product manufacturing, machinery, automotive, metallurgy and building materials industry. Chengdu's GRP increased from RMB1.8 trillion in 2020 to RMB2.1 trillion in 2022. Affected by the pandemic and tax refund, the Chengdu government's general budgetary revenue amounted to RMB172.2 billion in 2022, a YoY increase of 1.4%. Its fiscal balance ratio was 70.7%, which was at a moderate level. Chengdu's debt burden is manageable. In 2022, Chengdu's outstanding government debt increased to RMB464.1 billion with an increasing trend, accounting for 88.9% of its total fiscal revenue and 22.3% of its GRP.

Exhibit 4. Key Economic and Fiscal Indicators of Chengdu City

	2020FY	2021FY	2022FY
GRP (RMB billion)	1,771.7	1,991.7	2,081.8
GRP Growth (%)	4.0	8.6	2.8
General Budgetary Revenue (RMB billion)	152.0	169.8	172.2
General Budgetary Expenditure (RMB billion)	215.9	223.8	243.5
Local Government Debt (RMB billion)	344.0	404.3	464.1

Source: Statistic Bureau of Chengdu City, CCXAP research

Located in the northwest of Chengdu, with a total area of 1,208 square kilometers. Dujiangyan is known as an excellent tourist city in China. With its rich cultural heritage and beautiful natural landscapes, it attracts millions of tourists from all over the world every year. However, the industrial base of Dujiangyan is relatively weak, mainly focusing on mechanical manufacturing, food and beverage industries. Dujiangyan's GRP increased from RMB 44.2 billion in 2020 to RMB 48.4 billion in 2022, a YoY increase of 1.0% in 2022, and its GRP growth rate is lower than Sichuan Province and the national average. Affected by the economic slowdown and tax refund, Dujiangyan government's general budgetary revenue was RMB3.4 billion in 2022, a YoY decrease of 14.6%, of which tax revenue accounted for 61.3%. Dujiangyan has relatively good fiscal self-sufficiency, with an average general budgetary revenue/general budgetary expenditure ratio of 68% over the past three years. Dujiangyan's government debt balance has marginally declined over the past three years, but still has a relatively heavy debt burden, with outstanding debt accounting for 29.8% of its GRP in 2022.

Exhibit 5. Key Economic and Fiscal Indicators of Dujiangyan City

	2020FY	2021FY	2022FY
GRP (RMB billion)	44.2	48.4	48.4
GRP Growth (%)	4.1	7.1	1.0
General Budgetary Revenue (RMB billion)	3.6	4.0	3.4
General Budgetary Expenditure (RMB billion)	5.7	5.3	5.2
Local Government Debt (RMB billion)	15.1	14.5	14.4

Source: Statistic Bureau of Dujiangyan City, CCXAP research

Government's Willingness to Provide Support**Important role as the major infrastructure constructor and urban operator in Dujiangyan City**

In order to optimize the layout of state-owned capital, the Dujiangyan Government established CDID in 2020, which is the only primary platform in Dujiangyan City for consolidating regional assets and resources. CDID has 5 main subsidiaries and each with different positioning, including cultural and tourism, urban operation, industrial development, rural revitalization, and social livelihood. DSOC has a clear positioning of urban operation of Dujiangyan City. The Company is responsible for resettlement housing construction, infrastructure construction, and parking lot operation in Dujiangyan City. Considering the Company's high strategic significance to the development of Dujiangyan City, we believe the Company will not be easily replaced by other local state-owned enterprises in the foreseeable future.

The Company had successfully delivered a series of large-scale infrastructure projects and public welfare facilities over the past few years, such as roads, schools, hospitals, and detention center. The Company signs entrusting construction agreements with CDID, who would be responsible for raising project funds and paying for construction management fees. As of 31 December 2022, the Company had 2 infrastructure construction projects under construction, with a total estimated investment amount of RMB96.1 million and an outstanding

amount of RMB38.7 million. However, the Company's repurchase payment collection period is relatively prolonged. As of 31 December 2022, the book value of contract performance costs in the Company's inventory was RMB5.8 billion, which are mainly completed infrastructure construction projects that have not yet received repurchase payments.

The Company is also entrusted by the government to conduct the construction of resettlement housing and disaster reconstruction housing with self-raised funds. The Company achieves fiscal balance through government repurchase, or selling the remaining resettlement housing at market prices. As of 31 December 2022, the Company had 4 resettlement housing projects under construction or planning, with a total estimated investment amount of RMB228.5 million and an outstanding amount of RMB157.3 million. Since the Company's positioning has transformed from agent construction entity to urban operator, its infrastructure construction model has gradually changed from agent construction model to self-operation model. The sustainability of its public welfare projects is relatively volatile as it mainly depends on government planning.

Increasing exposure to commercial activities

In addition to public activities, DSOC is also involved in various commercial activities such as property sales, material trading, property leasing and management, car parking services and human resource services. We consider DSOC's commercial business exposure to be low, as its market-driven businesses account for lower than 15% of its total assets.

DSOC's property development business is market-oriented, as the Company is responsible for the construction of commercial property projects and their subsequent sales. As of 31 December 2022, the Company completed 1 major property development project, with a total investment amount of RMB320 million and received a sales amount of RMB219.8 million. The Company has 1 major commercial property development project under construction, with an estimated total investment amount of RMB2.6 billion and an outstanding amount of RMB1.9 billion. The large investment amount might exert great capital expenditure pressure on the Company. As the Company's property development business is market-driven, the sales income is greatly affected by the recovery of local real estate market.

In addition, the Company also engaged in the construction of self-operated projects, such as historic and cultural district commercial revitalization project, and technology utilization park construction project. However, the Company needs to construct these properties by self-raised funds, exerting certain capital expenditure pressure. As of 31 December 2022, it had 4 major self-operated projects under construction or planning, with a total estimated and uninvested amount investment of RMB1.3 billion.

As a company positioned in urban operation, DSOC also provides several commercial activities in Dujiangyan City, such as material trading, property leasing and management, carparking services and human resource services. The diversified business types provide certain supplementary income for the Company. The Company is involved in property leasing business, including supporting shops and commercial properties. Benefited by the low acquisition and operating cost, as well as the high occupancy rate, the gross profit margin of the Company's property leasing business remains at a relatively high level. DSCO also conducts car parking services in Dujiangyan City, including parking lots and temporary roadside parking spaces. Affected by the pandemic, the decrease in the number of visitors to Dujiangyan has led to a gradual decline in parking fee revenue. Although these commercial activities have brought stable income to the Company, the small operating scales limit their contributions to the Company's overall profit.

Given the Company's blueprint to develop its market-driven businesses, we believe the Company will expand

the scale of its commercial business exposure in the future. However, the business risk for commercial businesses is manageable as the urban operation business has relatively high business stability. In addition, we consider the initial investment in the construction of the commercial activities will be large, exerting certain capital expenditure pressure on the Company.

Solid track record of receiving government payments

DSOC has a track record of receiving payments from the Dujiangyan City Government. These payments take various forms, such as government subsidies and capital injections. From 2020-2022, the Company received a total of RMB166.4 million in government subsidies. The Company also regularly receives repurchase payments for its public policy projects. Given DSOC's important strategic role, we expect the Company will continue to receive support from the Dujiangyan City Government in the future.

Exhibit 6. Track Record of Government Support from 2020 to 2022

(RMB million)	2020FY	2021FY	2022FY
Government Subsidies	15	61	90
Capital Injections	-	-	100
Repurchase Payments	120	-	479
Total	135	61	669

Source: Company information, CCXAP research

Increasing debt burden and moderate asset liquidity

DSOC's total debt had increased from RMB5.7 billion at end-2020 to RMB7.9 billion as of 31 December 2022, its total capitalization increased from 34.1% to 41.1% over the same period. The increase in debt was mainly attributable to the expansion of the construction of public activities and commercial activities projects. As of 31 December 2022, the Company had 11 projects under construction or planning, with an expected investment of RMB4.2 billion and an outstanding amount of RMB3.5 billion. Given the Company's relatively large capital expenditure pressure, we expect the Company will maintain a relatively fast debt growth for the next 12-18 months.

Exhibit 7. Major Projects under Construction and Planning as of 31 December 2022

Project Types	No. of Projects	Budgeted	Invested	Outstanding
		Amount	Amount	Amount
(RMB million)				
Projects Under Construction				
Infrastructure Construction	2	96	39	57
Resettlement Housing	1	130	71	59
Self-Operating Projects	1	2	2	0
Property Development	1	2,571	641	1,930
Projects Under Planning				
Resettlement Housing	3	99	-	99
Self-Operating Projects	3	1,323	-	1,323
Total	11	4,221	753	3,468

Source: Company information, CCXAP research

Furthermore, DSOC has moderate asset liquidity. The Company's total asset mainly consists of inventories and receivables, which accounted for 85.3% of its total asset as of 31 December 2022. Inventories were mainly

undeveloped land and investment costs for its construction projects, while receivables were mainly unreceived payments from the agencies of government or other state-owned companies, all of which are considered low liquidity. As there were relatively large amounts of unreceived payments from the repurchased projects, we will pay attention to the payment collection.

Relatively high reliance on non-standard financing

DSOC has access to funding as reflected by its good banking relationships and access to the onshore debt capital market. As of 31 December 2022, it held total credit facilities of RMB6.2 billion and available credit facilities of RMB2.5 billion. The Company has also diversified its financing channel to the onshore debt capital market, including PPN and Corporate bonds, with an average coupon range of 6.3%. However, the Company has a relatively high reliance on non-standard financing. Around 30% of debt financing was provided by non-standard financing, including trust financing and asset management financing. It also plans to issue offshore bonds to broaden its financing channel and reduce its reliance on non-standard financing.

Medium exposure to contingent risks

DSOC has medium exposure to contingent risks due to its relatively large amount of external guarantees. As of 31 December 2022, its external guarantee amount was RMB3.8 billion, accounting for 33.3% of its net asset. All the external guarantees are provided to state-owned enterprises in Dujiangyan City. However, should a credit event occurs, the Company may face certain contingent risks, which could inversely impact its credit quality.

ESG Considerations

The Company is subject to environmental laws and regulations governing air pollution, noise emissions, hazardous substances, water and waste discharge and other environmental matters issued by the national governmental authorities. DSOC assumes environmental risks for its infrastructure projects. Such risks could be mitigated by conducting environmental studies and detailed planning prior to the commencement of projects and close supervision during construction.

DSOC is also exposed to social risks as it implements public-policy initiatives by building public infrastructure in Dujiangyan City. Demographic changes, public awareness and social priorities shape government's development strategy, and it will affect the government's propensity to support the Company.

The Company's governance considerations are also material as it is subject to oversight and reporting requirements to the local government, reflecting its public-policy role and status as a government-owned entity. DSOC believes that it is in compliance in all material respects with the applicable governmental regulations, rules and executive orders in each jurisdiction in which it operates. The Company maintains regular communication with local governments and regulatory authorities through its management team or representatives, ensuring compliance with the requirements and conditions for obtaining and maintaining the licenses, concessions, permits, or certificates.

Structural Consideration

DSOC's senior unsecured debt rating is equivalent to its long-term credit rating. We believe that government support will flow through the Company given its key roles in local infrastructure construction and urban operation in Dujiangyan City, thereby mitigating any differences in an expected loss that could result from structural subordination.

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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