

Credit Opinion

3 July 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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Changxing Urban Construction Investment Group Co., Ltd.

Initial credit rating report

CCXAP assigns long-term credit rating of BBB_g to Changxing Urban Construction Investment Group Co., Ltd., with stable outlook.

Summary

The BBB_g long-term credit rating of Changxing Urban Construction Investment Group Co., Ltd. (“CUCI” or the “Company”) reflects (1) Changxing County Government’s strong capacity to support, and (2) the local government’s extremely high willingness to support, based on our assessment of the Company’s characteristics.

Our assessment of Changxing County Government’s capacity to support reflects its status as the 50th Top 100 Economic Counties in China in 2022, with good economic strength and moderate fiscal metrics.

The rating also reflects the local government’s willingness to support, which is based on the Company’s (1) important role in undertaking public services in Changxing County; (2) sustainable public businesses given large projects in the pipeline; and (3) good track record of receiving government payments.

However, the Company’s rating is strained by (1) moderate commercial exposure; (2) medium contingent liability risk from external guarantees provided to other local SOEs; and (3) relatively high debt leverage and moderate asset liquidity.

The stable outlook on CUCI’s rating reflects our expectation that the local government’s capacity to support will remain stable, and the Company will maintain its important role in the public welfare functions in Changxing County.

Rating Drivers

- Important role in undertaking public services in Changxing County
- Sustainable public businesses given large projects in the pipeline
- Moderate exposure to commercial activities
- Relatively high debt leverage and moderate asset liquidity Large
- Medium contingent liability risk from external guarantees provided to other local SOEs
- Good access to funding

Rating Sensitivities

What could upgrade the rating?

The rating could be upgraded if (1) the local government's capacity to support strengthens; or (2) the Company's characteristics change in a way that strengthens the local government's willingness to support, such as improvement in debt management or assets quality.

What could downgrade the rating?

The rating could be downgraded if (1) the local 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 decrease in its strategic significance; decrease in government payments; or increase in exposure to commercial activities.

Key Indicators

	2020FY	2021FY	2022FY
Total Asset (RMB billion)	62.5	70.6	76.5
Total Equity (RMB billion)	29.9	32.7	32.9
Total Revenue (RMB billion)	2.3	3.2	3.3
Total Debt/Total Capital (%)	47.3	50.0	52.7

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

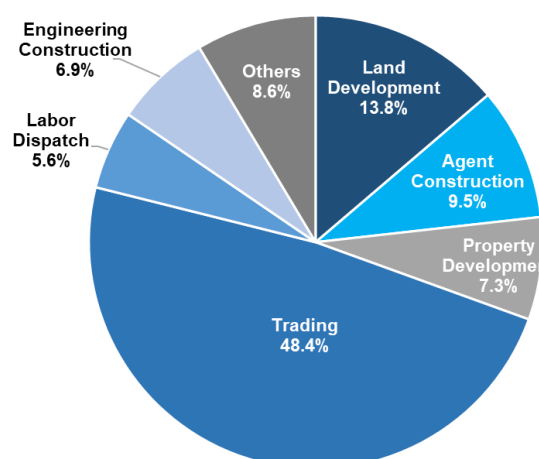
Source: CCXAP research

Corporate Profile

CUCI, formerly known as Changxing Urban Construction Co., Ltd., was established by Changxing County Urban Construction Development Corporation on 21 December 2007, which was controlled by the Changxing Municipal Government. CUCI is one of the key infrastructure investment and financing companies in Changxing County, Huzhou City. The Company mainly engages in trading, infrastructure construction, property development, primary land consolidation and city operations, including water supply, education, and car park operation.

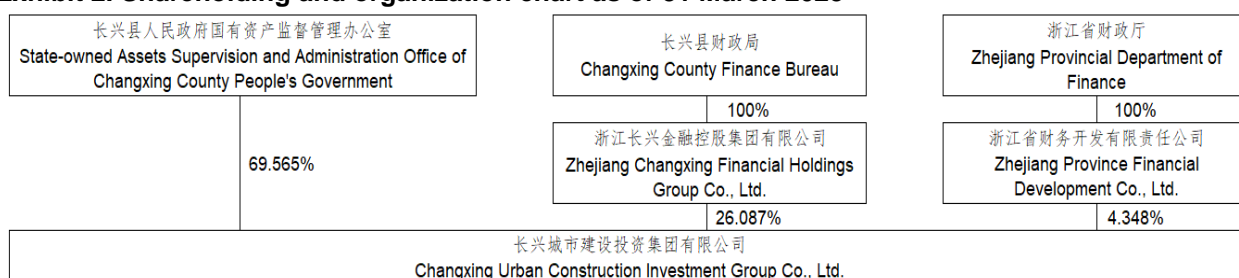
As of 31 December 2022, the State-owned Assets Supervision and Administration Office of Changxing County People's Government ("Changxing SASAO") and Zhejiang Changxing Financial Holdings Group Co., Ltd. held 69.6% and 26.1% of the Company's shares respectively, while Zhejiang Province Financial Development Co., Ltd. held the remaining 4.3%. Changxing SASAO is the ultimate controller of the Company. The Company's paid-in capital was RMB2.3 billion.

Exhibit 1. Revenue structure in 2022



Source: Company information, CCXAP research

Exhibit 2. Shareholding and organization chart as of 31 March 2023



Source: Company information, CCXAP research

Rating Considerations

Government Capacity to Support

We believe that Changxing County Government has a strong capacity to provide support as reflected by its status as the 50th Top 100 Economic Counties in China in 2022, with good economic strength and moderate fiscal metrics. However, the capacity to support is constrained by its relatively weak debt profile.

Located in the northern part of Zhejiang Province, Huzhou City is the node city connecting the north and south areas of the Yangtze River Delta region. In 2022, Huzhou City recorded a gross regional product (“GRP”) of RMB385.0 billion, increasing by 3.3% year-over-year (“YoY”). Due to the COVID-19 pandemic and tax refund factor, Huzhou Municipal Government’s general budgetary revenue decreased from RMB41.4 billion in 2021 to RMB38.7 billion in 2022. Its fiscal balance remained at a moderate level, with general budgetary revenue to general budgetary expenditure ratio of 64.3% in 2022. However, Huzhou Municipal Government’s debt burden was relatively large with an outstanding direct government debt of RMB118.9 billion at end-2022, accounting for 30.9% of its GRP and 85.7% of its total fiscal revenue.

Exhibit 3. Key Economic and Fiscal Indicators of Huzhou City

	2020FY	2021FY	2022FY
GRP (RMB billion)	320.1	364.5	385.0
GRP Growth (%)	3.3	9.5	3.3
General Budgetary Revenue (RMB billion)	33.7	41.4	38.7
General Budgetary Expenditure (RMB billion)	48.4	52.4	60.2
Local Government Debt (RMB billion)	83.7	102.3	118.9

Source: Statistics Bureau of Huzhou City, CCXAP research

Changxing County is the second largest county, in terms of GRP, in Huzhou City. According to CCID Consulting, Changxing County ranked 50th Top 100 Economic Counties in China in 2022. The pillar industries of Changxing County are textile, cement and battery manufacturing industries. Changxing County has improved its industrial structure by strategically promoting emerging industries, such as new type battery and new energy vehicle, and has developed a sizeable leisure facility, namely Longmont, with a total investment of around RMB25 billion. In 2022, Changxing County recorded a GRP of RMB85.3 billion, increasing by 4.2% YoY. We believe that the sustainable economic development of Changxing County provides a sound external environment for the Company's business development. Due to tax refunds and the pandemic, Changxing County Government's general budgetary revenue decreased slightly from RMB8.3 billion in 2021 to RMB8.2 billion in 2022, tax revenue accounted for 91.7% of the general budgetary revenue in 2022. Changxing County had a large debt burden, as of end-2022, Changxing County Government's outstanding direct debt amounted to RMB19.1 billion, about 22.4% of its GRP and 91.3% of its total fiscal revenue.

Exhibit 4. Key Economic and Fiscal Indicators of Changxing County

	2020FY	2021FY	2022FY
GRP (RMB billion)	70.2	80.1	85.3
GRP Growth (%)	2.6	9.5	4.2
General Budgetary Revenue (RMB billion)	6.8	8.3	8.2
General Budgetary Expenditure (RMB billion)	9.0	10.2	10.5
Local Government Debt (RMB billion)	16.4	17.7	19.1

Source: Statistics Bureau of Changxing County, CCXAP research

Government Willingness to Support**Important role in undertaking public services in Changxing County**

There are four major financing and investment companies to support the development and operation of Changxing County. Each has a clear position under the local government's planning. Among them, CUCI is one of the most important local infrastructure investment and financing companies in Changxing County and has mainly undertaken public activities such as infrastructure construction, primary land consolidation, and water supply.

CUCI is one of the key infrastructure constructors with a strong regional position in Changxing County. Currently, the Company is mainly responsible for the infrastructure construction in the old town district and Longshan new district under the agent-construction model, mainly undertaking school, road, renovation of shantytown, garbage station, and sewage treatment projects in the past three years. As of 31 December 2022, the Company had 13 infrastructure construction projects under construction or planning, with a total estimated investment of RMB3.9 billion, and an uninvested amount of RMB468 million. Overall, the infrastructure construction business is sustainable given the considerable construction projects in the pipeline.

CUCI also has a strong regional position in the primary land consolidation of Changxing County. The Company's business scope of primary land consolidation business covers Longshan New District, Huilongshan New District and the old town district. As of 31 December 2022, the Company completed the consolidation of 473.8 mu land parcels that have not yet been sold, and the Company had 11,387 mu land parcels under development. Besides, there was one consolidation project under planning with an area of 280 mu and a total estimated investment of RMB224 million. The Company has sufficient project reserves for its primary land consolidation, but the primary land consolidation could be greatly affected by the land policy and planning of the local government.

The Company participated in water supply projects through its subsidiary, such projects include production and construction of water supply and drainage, and installation of water engineering. Before 2022, CUCI's water supply business mainly covered 224 square kilometres in Lincheng Town and the eastern region of Changxing County. After the acquisition of a new water supply plant in early 2022, the operating area of its water supply business has expanded by 134 square kilometres to 358 square kilometres. The Company has 2 water supply plants including Shuikou Water Plant and Qingquan Water Plant. The Company also has 3 water supply stations with 587 kilometers network and a daily water supply capacity of around 70,000 tons/day, serving 46,000 residents. With the consolidation of other water supply companies in Changxing County and the completion of its developing projects, we expect that the Company's public welfare function will be strengthened, suggesting stronger strategic importance and stronger governmental support.

Overall, the Company has made significant contributions to the regional development of Changxing County, we expect that the strategic position of the Company will be maintained in the foreseeable future.

Good track record of receiving ongoing government payments

The local government provides strong support, in terms of capital injection, assets injection and subsidies, to the Company to support its business development. The local government has injected several assets into the Company, such as Changxing Construction Property Development Co., Ltd. ("CCPD") (social housing development business), and Changxing Qingquan Water Supply Co., Ltd. (water supply business), which helped strengthen its business profile. In December 2020, Changxing Communications Investment Group Co., Ltd. transferred 9.53% equity shares of Yongxing Construction Development Co., Ltd. ("Yongxing") to CUCI. After the transfer, the Company had 51% equity shares of Yongxing. Besides, the Company's business scope of infrastructure construction and primary land development expanded to Longshan New District, and its position in Changxing County has been further strengthened.

From 2020 to 2022, the Company received RMB2.4 billion in government subsidies and a fiscal interest discount of RMB1.3 billion to support its operation. The local government also injected sandstone assets operation rights and outdoor advertising spaces franchise rights within the main urban area of Changxing County, as well as real properties, cash and seedling assets into the Company, increasing its capital reserve of RMB2.1 billion from 2020 to 2022.

Moderate exposure to commercial activities

Apart from the primary business segments, CUCI has also diversified into other market-oriented businesses since 2017, such as trading, property development, and sandstone mining.

CUCI has engaged in property development since December 2017, after the government transferred 51.05% of CCPD's shares to the Company. As of 31 December 2022, the Company held properties with a remaining saleable area of 122.5 thousand sqm, which is sufficient to support the Company's revenue in the short run. In

addition, the Company had 2 property projects under construction and one property project under planning, with a total estimated investment of RMB6.5 billion, and an uninvested amount of RMB3.0 billion. The larger investment will bring certain capital expenditure pressure to the Company, and uncertainty exists in this business as it is highly subject to local government planning and the local real estate market.

For the trading segment, the Company mainly provided building materials and coals to local corporates. It is still exposed to concentration risk as the top five suppliers and consumers accounted for around 96.9% and 66.9% of its purchasing and sales amount, respectively, increasing uncertainties in this business.

As CUCI gained a 30-year franchise right for sandstone mining in Changxing County, it was newly engaged in the sandstone mining business in 2020. The Company's sandstone mining covers total sandstone reserves of 146.3 million tons and exploitable amounts of 65.0 million tons. Due to high amortization costs and short operation time, the Company incurred large gross losses from the business, dragging down its overall profitability.

CUCI started its education business in 2019, after the injection of two secondary schools and two primary schools from the government. However, according to government planning, after the four schools have been transferred out of the Company in 2022, the tuition income in 2022 was RMB39.6 million and the education business is no longer the main business of the Company.

CUCI has engaged in car park operations since November 2018. As of 31 December 2022, the Company owned 2,445 on-street parking spaces and 7 parking lots in operation. The Company also has 11 parking lots under development, which are expected to provide 4,316 parking spaces and 500 charging piles to the Company. The Company earns rental income by leasing self-owned investment properties, including commercial complexes and residential properties.

Overall, the proportion of commercial business assets is less than 20% of the Company's total assets, indicating that the overall commercial business risk is moderate. We also expect that the diversified business layout can help mitigate the Company's business risk and enrich its income source. However, some of these businesses have a low-profit margin, which has adversely affected the Company's profitability, and we will continue to monitor the operation of the related businesses.

Relatively high debt leverage and moderate asset liquidity

The Company's total debt continued to increase in the past three years as ongoing investment needs. From 2020 to 2022, the Company's total debt increased from RMB27.0 billion to RMB36.6 billion, and its total capitalization ratio was at a relatively high level of around 52.7% in 2022. Given its expanding projects, we expect the Company will have great pressure on capital expenditure in the future.

Exhibit 5. Projects under construction and planning as of 31 December 2022

Project type	No. of projects	Budgeted amount (RMB million)	Invested amount (RMB million)	Outstanding amount (RMB million)
Projects Under Construction				
<i>Infrastructure Construction</i>	14	3,932	3,502	430
<i>Primary Land Development</i>	6	-	1,988	-
<i>Property Development</i>	2	4,900	3,504	1,396
<i>Self-owned Projects</i>	1	1,144	1,096	48
Projects Under Planning				
<i>Infrastructure Construction</i>	3	380	-	380
<i>Property Development</i>	1	1,600	-	1,600
<i>Primary Land Development</i>	1	224	-	224
Total	28	12,180	10,090	4,078

Source: Company information, CCXAP Research

The Company's asset liquidity was moderate as they were mainly inventories with weak liquidity. As of 31 December 2022, the inventories amounted to RMB34.9 billion, accounting for 45.6% of total assets, and mainly consisted of construction costs caused by infrastructure construction projects. The moderate liquidity asset may undermine the Company's financing flexibility, which is credit negative.

Good access to funding

The Company has good access to funding. The Company had total credit facilities of RMB24.2 billion, of which the unutilized amount was about RMB4.5 billion as end-2022. The Company also had good access to the debt markets. From 2022 to 2023, the Company and its subsidiaries raised RMB7.7 billion through the onshore debt market; and had raised USD535 million through the offshore debt market. In addition, the Company's financing channel is highly dependent on the capital market with outstanding bonds accounting for 51.2% of its total debt, and bank loans accounting for 36.5%. Besides, the Company's exposure to non-standard financing is relatively low, accounting for about 10% of total debt at end-2022.

Medium contingent liability risk from external guarantees provided to other SOEs

The Company is exposed to a medium contingent liabilities risk. At end-2022, the Company recorded an external guarantee amount of RMB11.7 billion, accounting for 35.6% of its total equity. Those guaranteed entities are the state-owned enterprises ("SOE") in Changxing County, without counter-guarantee measures, the credit risk of the Company and other local SOEs might be heightened if one guaranteed entity suffers from credit issues.

ESG Considerations

CUCI is exposed to environmental risks because it has undertaken infrastructure construction and utility projects. Such risks could be moderated by conducting environmental studies and planning before the commencement of projects, and close supervision during the construction phase. Since 2021, CUCI issued two green USD bonds and three green corporate bonds on both onshore and offshore markets. The issuance of green bonds by CUCI is an important example of promoting the innovative development of green finance, which can reduce its environmental risks.

In terms of social concerns, CUCI plays a crucial role in the social welfare of the residents in Changxing County by providing utility services, including water supply, sewage treatment, education, and car park operation. As an important state-owned entity in Changxing County, the Company has also launched multiple measures to ensure the provision of utility and daily needs of the residents during the pandemic control period.

In terms of corporate governance, CUCI has established a sound and effective internal control framework, and has also set up a corporate governance structure, with the shareholders, directors, supervisors, senior management team and internal departments performing their duties collectively and efficiently. The Company is subject to oversight and reporting requirements to the Changxing SASAO, which has full control and supervision of the Company's operation.

Structural considerations

We did not notch CUCI's senior unsecured debts rating for structural subordination, reflecting our expectation that in the event of financial distress, the local government will likely provide support to the Company, thereby increasing the recovery prospects for its creditors. We also see that the structural subordination risk is mitigated by CUCI's important role in undertaking public services in Changxing County, thus we expect that government support will be provided to the Company to preserve its ownership of such assets.

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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