

Credit Opinion

21 July 2023

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

Analyst Contacts

Peter Chong +852-2860 7124
Assistant Director of Credit Ratings
peter_chong@ccxap.com

Karissa Du +852-2860 7126
Credit Analyst
karissa_du@ccxap.com

Elle Hu +852-2860 7120
Executive Director of Credit Ratings
elle_hu@ccxap.com

**The first name above is the lead analyst for this rating and the last name above is the person primarily responsible for approving this rating.*

Client Services

Hong Kong +852-2860 7111

Zhaoqing Gaoyao District State-Owned Assets Operation Co., Ltd.

Surveillance credit rating report

CCXAP affirms Zhaoqing Gaoyao District State-Owned Assets Operation Co., Ltd.'s long-term credit rating of BBB_g-, with stable outlook.

Summary

The BBB_g- long-term credit rating of Zhaoqing Gaoyao District State-Owned Assets Operation Co., Ltd. ("GSAO" or the "Company") reflects the Gaoyao District Government's (1) relatively strong capacity to provide support, and (2) extremely high willingness to provide support to the Company, based on our assessment of the Company's characteristics.

Our assessment of the Gaoyao District Government's capacity to provide support reflects its important economic status in Zhaoqing City, relatively good investment potential, and ongoing economic growth.

The rating also reflects the local government's willingness to provide support, which is based on the Company's (1) important position in infrastructure construction and water supply of Gaoyao District; and (2) good track record of receiving governmental payments.

However, the Company's rating is constrained by the Company's (1) moderate asset quality; and (2) high reliance on non-standard fundings.

The stable outlook on GSAO's rating reflects our expectation that the local government's capacity to provide support will remain stable, and that the Company will maintain its important position in Gaoyao District and continue to receive ongoing government support.

Rating Drivers

- Important position in infrastructure construction and water supply of Gaoyao District
- Good track record of receiving governmental payments
- Medium exposure to commercial activities, with manageable commercial risks
- Manageable debt leverage but moderate asset quality
- High reliance on non-standard fundings, alleviated by sufficient standby liquidity and access to debt capital market

Rating Sensitivities

What could upgrade the rating?

The rating could be upgraded if (1) the local government's ability to provide support strengthens; and (2) the Company's characteristics change in a way that strengthens local government's willingness to provide support, such as improvement in access to funding and asset quality.

What could downgrade the rating?

The rating could be downgraded if (1) the local government's ability to provide support weakens; or (2) the Company's characteristics change in a way that decrease the local government's willingness to provide support, such as reduced regional significance or increase in exposure to commercial activities.

Key Indicators

	2020FY	2021FY	2022FY
Total Asset (RMB billion)	18.6	18.7	22.4
Total Equity (RMB billion)	9.7	9.9	11.4
Total Revenue (RMB billion)	0.5	1.0	2.0
Total Debt/Total Capital (%)	41.7	34.4	36.3

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

Source: CCXAP research

Corporate Profile

Founded in 1994, GSAO is a key state-owned enterprise in Gaoyao District of Zhaoqing City. The Company is mainly engaged in public policy businesses such as infrastructure construction and water supply, and commercial businesses such as civil explosive sales, provision of security services, meat processing, and driving training. As of 31 March 2023, as the ultimate controlling shareholder of the Company, State-owned Assets Supervision and Administration Bureau of Gaoyao District of Zhaoqing City ("Gaoyao SASAB") held 90% of the Company's equity interests, while the Department of Finance of Guangdong Province held the remaining 10%. Gaoyao SASAB has decided to transfer its 90% equity interests of GSAO to Zhaoqing Gaosheng City Investment Development Co., Ltd, which has become the largest shareholder of the Company; however, the registration of shareholder changes has not been completed.

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Exhibit 1. GSAO's revenue structure in 2022

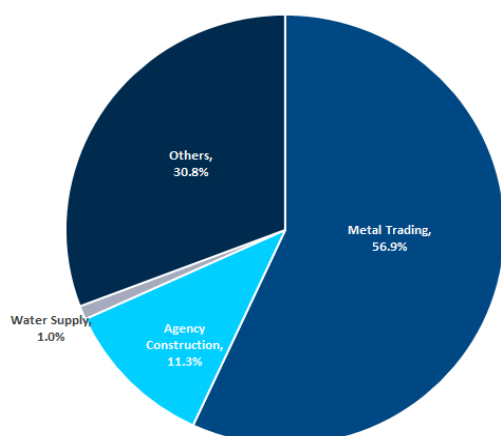
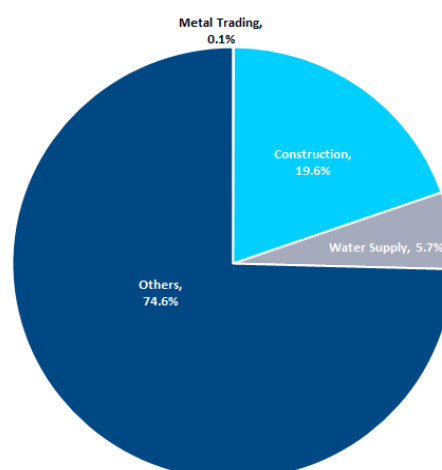
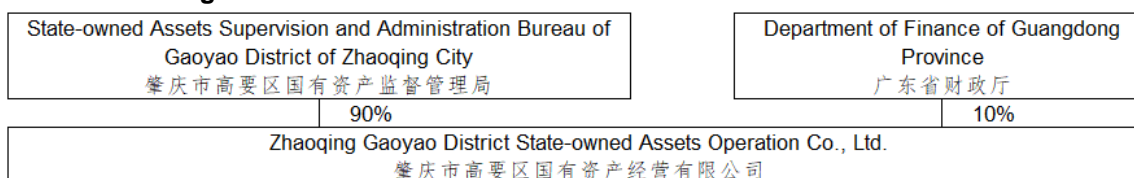


Exhibit 2. GSAO's gross profit structure in 2022



Source: Company information, CCXAP research

Exhibit 3. Shareholding Chart as of 31 March 2023



Source: Company information, CCXAP research

Rating Considerations

Government's Capacity to Provide Support

We believe that the Gaoyao District Government has relatively strong capacity to provide support, given its important economic status in Zhaoqing City, relatively good investment potential, and ongoing economic growth.

Guangdong Province is one of the most economically developed provinces in China, and its comprehensive economic strength outperforms other provinces. In 2022, the gross regional product ("GRP") of Guangdong Province was RMB12.9 trillion, ranking first among all provinces in China, with a year-on-year ("YoY") increase of 1.9%. In 2022, its general budgetary revenue reached RMB1.3 trillion, ranking first in China for more than 30 consecutive years.

Located in the western part of Guangdong Province, Zhaoqing City is the largest inland city in the Guangdong Hong Kong-Macao Greater Bay Area ("Greater Bay Area"). Zhaoqing City has a well-developed transportation network, forming a comprehensive transportation hub with "one intercity railway, two express links, seven expressways, and one golden waterway". In recent years, Zhaoqing City has developed three industrial clusters valued over RMB100 billion, namely new energy vehicles, advanced equipment manufacturing, and energy conservation and environmental protection. In 2022, the GRP of Zhaoqing City increased by 1.1% YoY to RMB270.5 billion, ranking 12th among 21 cities in Guangdong Province. With the continuous development of the regional economy, Zhaoqing Municipal Government's general budgetary revenue had increased from RMB12.5 billion in 2020 to RMB16.1 billion in 2022, of which tax income accounted for 56.8% on average during

the period. However, the fiscal balance of Zhaoqing City is relatively weak, averaging at 35.4% from 2020 to 2022. As at end-2022, Zhaoqing's local government debt balance was RMB99.6 billion, accounting for 36.8% of GRP.

Exhibit 4. Key Economic and Fiscal Indicators of Zhaoqing City

	2020FY	2021FY	2022FY
GRP (RMB billion)	231.2	265.0	270.5
GRP Growth (%)	3.0	10.5	1.1
General Budgetary Revenue (RMB billion)	12.5	14.7	16.1
General Budgetary Expenditure (RMB billion)	43.1	39.7	39.7
Local Government Debt (RMB billion)	53.3	87.7	99.6

Source: Statistics Bureau of Zhaoqing City, CCXAP research

Gaoyao District is located in the central part of Guangdong Province, belonging to the Pearl River Delta, Guangzhou-Foshan-Zhaoqing Economic Circle and Zhaoqing Economic Development Center. Gaoyao District has a relatively good investment potential, ranking 43rd by investment potential among Top 100 districts in China according to the research results of High-quality Development Index of China's Small- and Medium-sized Cities in 2022. Gaoyao District has formed an industrial layout with auto parts and hardware processing industries as the core industries, supplemented by advanced equipment manufacturing, chemical industry and health and leisure industries. In 2022, the GRP of Gaoyao District was RMB54.2 billion, a YoY increase of 3.5%, ranking first among all districts in Zhaoqing City. In the same year, Gaoyao District Government recorded a general budgetary revenue of RMB2.8 billion, of which tax income accounted for 43.3%, indicating moderate fiscal stability. In addition, its fiscal balance ratio was modest at 52.2%. In terms of debt profile, the outstanding debt balance of the Gaoyao District Government was RMB8.9 billion at end-2022, accounting for 16.5% of GRP.

Exhibit 5. Key Economic and Fiscal Indicators of Gaoyao District

	2020FY	2021FY	2022FY
GRP (RMB billion)	44.0	50.7	54.2
GRP Growth (%)	3.2	11.5	3.5
General Budgetary Revenue (RMB billion)	1.8	2.2	2.8
General Budgetary Expenditure (RMB billion)	5.6	5.2	5.4
Local Government Debt (RMB billion)	3.9	7.6	8.9

Source: Statistics Bureau of Gaoyao District, CCXAP research

Government's Willingness to Provide Support

Important position in infrastructure construction and water supply of Gaoyao District

There are two key companies undertaking infrastructure construction in Gaoyao District, namely GSAO and Zhaoqing Gaoyao Construction Investment Development Group Co., Ltd. ("GJID"), each has a clear position under the local government's planning. The business scope of GJID is mainly concentrated in the new urban area of Gaoyao District and Jinli High-tech Zone, while the business scope of GSAO is mainly concentrated in the old urban area of Gaoyao District. GSAO plays an important strategic role in supporting and promoting the urbanization and industrialization of Gaoyao District. Since its establishment, the Company has undertaken numerous key municipal infrastructure projects in Gaoyao District, including municipal roads, and urbanization construction. As of 31 December 2022, the Company had completed 2 key infrastructure construction projects with a total investment of RMB943.2 million. We believe that GSAO's important role in the development of

Gaoyao District and its public welfare functions are unlikely to be replaced in the short-to-medium term.

GSAO continued to conduct infrastructure construction projects under agency construction model, with certain future capital pressure. As of 31 December 2022, the Company had invested RMB1.6 billion into 4 key agency projects under construction, with uninvested amount of RMB1.8 billion. However, there is no agency project under planning as the Company is switching its business focus from agency infrastructure construction to self-built construction. The sustainability of agency construction business is subject to uncertainty.

GSAO's water supply business has a regional dominant position as it covers the main area of Gaoyao District, except for some towns. In 2022, the Company distributed water of over 60 million tons to 118,300 households in Gaoyao District via five water plants and pipe network of 263 kilometers. The water supply service will cover the whole Gaoyao District when construction completion of a new water plant, which can further enhance its market position and revenue generation. In 2022, the Company achieved a revenue of RMB20.0 million from the water supply business. We expect the water supply business will continue to provide stable income to the Company.

In addition, the Company has no longer involved in the grain sales business since June 2022, as its subsidiary Zhaoqing Gaoyao District Yufeng Grain Reserve Co., Ltd. was transferred out of the Company. We believe the asset transfer will not materially influence the Company's credit profile, as the grain sales business only accounts for small portion of its asset and revenue.

Good track record of receiving government payments

GSAO has a good track record of receiving ongoing government payments, in the form of operating subsidies, capital injections, project payments, and high-quality asset transfers. After years of capital injections by the Gaoyao District Government, the Company's registered capital had increased from the original RMB10.0 million to RMB178.0 million. The local government also transfers high-quality assets to the Company to enhance its asset strength and revenue. In 2022, the Gaoyao District Government transferred rental properties of RMB2.0 billion to the Company, which can generate stable rental income. From 2020 to 2022, the Company received RMB787.9 million in government subsidies to support its operation and project construction. The Company also regularly receives agency project payments from the local government, totaling RMB594.3 million over the past three years. Given its important strategic position in Gaoyao District, we expect the local government will provide ongoing and stable support to the Company.

Medium exposure to commercial activities, with manageable commercial risks

GSAO also participates in a number of commercial activities, such as self-built project construction and metal trading. The Company has moderate exposure to commercial activities with the proportion of commercial assets accounting for less than 20% of its total assets. Nonetheless, we expect that the overall commercial risk is manageable, as some of the commercial businesses provide stable income and reasonable gross profit to the Company.

The Company has participated in self-built project construction, including industrial park construction, pipe network expansion, and land reclamation. As of 31 December 2022, the Company had invested RMB1.3 billion into 7 self-built projects under construction, with uninvested amount of about RMB377 million. It also plans to construct several self-operating projects, such as charging piles, parking lots, and gas stations. As of 31 December 2022, the Company had 4 key self-built projects under planning, with total estimated investment of

RMB3.0 billion. Although these self-built projects exert certain capital expenditure pressure to the Company, they will provide stable operating income to the Company after completion of construction.

GSAO has started metal trading business since 2021, with trading products mainly including electrolytic copper and aluminum ingot. The metal trading business is the main income source of the Company. In 2022, it generated revenue from metal trading business of RMB1.1 billion, accounting for 56.9% of its total revenue, but recording a low gross profit margin of less than 1%. However, the metal trading business is subject to concentration risk due to its relatively high reliance on top 5 customers and suppliers.

GSAO is also engaged in several market-oriented businesses, including sales of civil explosives, provision of security services, meat processing, sales of fuel gas, and driving training businesses. However, the income scale of these businesses is small, totaling RMB127 million in 2022, and does not contribute much to the Company's revenue.

As the local government transferred industrial premises of RMB2.0 billion to the Company in 2022, it newly engages in property leasing business and will generate rental income this year. In addition, the Company acquired two mines in a joint venture with private enterprises in late 2021. It is expected that the two mines would provide stable annual income of about RMB60 million to the Company after completion of construction. Therefore, we expect the Company's exposure to commercial activities will increase gradually in the next 12 to 18 months.

Manageable debt leverage but moderate asset quality

In spite of ongoing financing for the construction projects, GSAO's debt leverage remains at a manageable level. As of end-2022, the Company's total debt amounted to RMB6.5 billion, with total capitalization ratio of 36.3%. However, the Company's short-term debt has increased significantly. Its short-term debt increased from RMB358.6 million at end-2020 to RMB3.6 billion at end-2022, accounting for 55.1% of total debt, indicating a higher debt maturity pressure. We expect the Company will continue to rely on external financing to meet its future capital expenditures and its debt leverage will increase in the next 12 to 18 months.

Exhibit 6. Projects under construction and planning as of 31 December 2022

Project Type	Budgeted Amount (RMB billion)	Invested Amount (RMB billion)	Outstanding Amount (RMB billion)
Projects under construction	5.1	3.0	2.1
Projects under planning	3.0	-	3.0
Total	8.1	3.0	5.1

Source: Company information, CCXAP research

GSAO's asset liquidity is moderate as its assets mainly consist of total receivables and inventories, both with low liquidity. As of 31 December 2022, the Company's total receivables and inventories accounted for 65.8% of total assets. The Company's inventories are mainly land use rights and infrastructure construction costs, and the total receivables are mainly unreceived project payments from Gaoyao SASAB and other local state-owned investment or construction companies. The moderate asset liquidity may undermine the Company's financing flexibility.

High reliance on non-standard fundings, alleviated by sufficient standby liquidity and access to debt capital market

GSAO is highly reliant on non-standard fundings, such as financial leases and trusts, which may increase its refinancing risk. As of 31 December 2022, the Company's non-standard debts accounted for about 45% of its total debt, resulting in relatively high comprehensive financing cost of about 7%. We believe the Company's refinancing risk can be partially alleviated by its sufficient standby liquidity and access to debt capital market. As of 31 December 2022, the Company obtained total credit facilities of RMB12.0 billion, with unutilized portion of RMB8.5 billion. In 2021, it raised USD48 million via the offshore bond market, with a coupon rate of 1.9%. It also plans to issue PPNs, USD bonds, and onshore corporate bonds to diversify its financing channel and lower the proportion of non-standard debts.

ESG Considerations

GSAO faces environmental risks because it has undertaken infrastructure development projects. Such risks could be moderated by conducting environmental studies and planning prior to the start of the projects, and close monitoring during the construction phase.

GSAO bears social risks as it implements public policy initiatives by undertaking infrastructure construction projects in Gaoyao District. Demographic changes, public awareness and social priorities shape the Company's development targets and ultimately affect the local government's willingness to support the Company.

GSAO's governance considerations are also material as the Company is subject to oversight by the Gaoyao District 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 \(July 2022\)](#).

Appendix

Exhibit 7. Peer Comparison in 2022

	Zhaoqing Gaoyao District State-Owned Assets Operation Co., Ltd.	Zhaoqing Gaoyao Jiantou Investment and Development Group Co., Ltd.
Long-Term Credit Rating	BBB _g -	BBB _g -
Shareholder	State-owned Assets Supervision and Administration Bureau of Gaoyao District of Zhaoqing City (90%); Department of Finance of Guangdong Province (10%)	Zhaoqing Gaosheng City Investment Development Co., Ltd
Positioning	Responsible for engineering project construction including development of parks, infrastructure construction, and shantytown reconstruction in old urban area of Gaoyao District.	Responsible for urban public infrastructure construction; civil engineering construction and landscaping engineering construction in new town of Gaoyao District and Jinli High-tech Zone.
Total Asset (RMB billion)	22.4	17.0
Total Equity (RMB billion)	11.4	6.9
Total Revenue (RMB billion)	2.0	1.6

Total Debt/Total Capital (%)	36.3	53.7
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All ratios and figures are calculated using CCXAP's adjustments.
Source: CCXAP research

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China Chengxin (Asia Pacific) Credit Ratings Company Limited

Address: Suites 1904-1909, 19/F, Jardine House,
1 Connaught Place, Central, Hong Kong

Website: www.ccxap.com

Email: info@ccxap.com

Tel: +852-2860 7111

Fax: +852-2868 0656