

## Credit Opinion

22 October 2024

### Ratings

Senior Unsecured Debt Rating	BBB <sub>g</sub>
Long-Term Credit Rating	BBB <sub>g</sub>
Outlook	Stable
Category	Corporate
Domicile	China
Rating Type	Solicited Rating

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## Luoyang Guoxing Investment Holding Group Co., Ltd.

### Initial credit rating report

**CCXAP assigns first-time long-term credit rating of BBB<sub>g</sub> to Luoyang Guoxing Investment Holding Group Co., Ltd., with stable outlook.**

### Summary

The BBB<sub>g</sub> long-term credit rating of Luoyang Guoxing Investment Holding Group Co., Ltd. ("LYGX" or the "Company") reflects Mengjin District Government's (1) strong capacity to provide support, and (2) extremely high willingness to provide support based on our assessment of the Company's characteristics.

Our assessment of Mengjin District Government's capacity to support reflects its relatively good economic strength, with ongoing economic growth and good fiscal stability. Mengjin District's gross regional product ("GRP") has ranked top among all the districts or counties in Luoyang City for years.

The rating also reflects the local government's willingness to support, which is based on the Company's (1) important role in infrastructure construction and urban operation of Mengjin District; and (2) good track record of receiving government support.

However, the rating is constrained by the Company's (1) increasing exposure to commercial activities; (2) increasing debt burden; and (3) moderate asset liquidity.

The stable outlook on LYGX's rating reflects our expectation that the Mengjin District Government's capacity to provide support will be stable, and the Company's characteristics such as its important role in infrastructure construction and urban operation of Mengjin District will remain unchanged over the next 12 to 18 months.

## Rating Drivers

- Important role in infrastructure construction and urban operation of Mengjin District
- Good track record of receiving government support
- Increasing exposure to commercial activities
- Increasing debt burden and moderate asset liquidity
- Fair access to funding channels

## Rating Sensitivities

### What could upgrade the rating?

The rating could be upgraded if (1) Mengjin 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 diversified the financing channels.

### What could downgrade the rating?

The rating could be downgraded if (1) Mengjin 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 provide support, such as reduced policy significance or increased exposure to contingent liabilities.

## Key Indicators

	2021FY	2022FY	2023FY	2024H1
Total Asset (RMB billion)	7.8	8.0	24.0	24.7
Total Equity (RMB billion)	4.9	5.1	19.0	19.1
Total Revenue (RMB billion)	0.7	0.9	1.5	0.7
Total Debt/Total Capital (%)	36.5	34.9	16.5	17.1

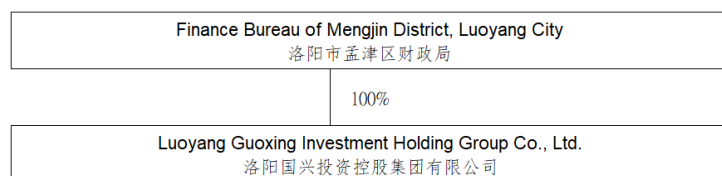
All ratios and figures are calculated using CCXAP's adjustments.

Source: Company data, CCXAP research

## Corporate Profile

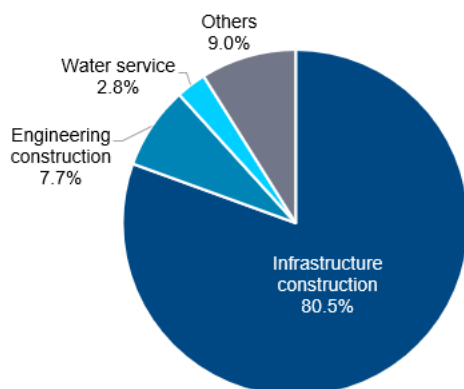
Established in 2016, LYGX is the largest local infrastructure investment and financing companies ("LIIFCs") by total assets in Mengjin District, Luoyang City. In accordance with the economic and industrial development plan of Mengjin District, the Company serves as the most important comprehensive state-owned capital investment and operation in Mengjin District. LYGX is mainly responsible for infrastructure construction and urban operation in Mengjin District, including water supply and rural revitalization. The Company has also diversified into other commercial activities, including self-operated construction, pipeline operation, property management, engineering construction, tourist attraction operation, and factoring. In 2023, the Finance Bureau of Mengjin District, Luoyang City ("Finance Bureau of Mengjin District") provided major capital injection to the Company including cash, equity and assets, enhancing the Company's capital strength significantly. As of 30 June 2024, the Company was wholly owned and controlled by the Finance Bureau of Mengjin District; the total asset of the Company was RMB24.7 billion.

### Exhibit 1. Shareholding chart as of 30 June 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 that the Mengjin District Government has a strong capacity to provide support, reflecting its relatively good economic strength, with ongoing economic growth and good fiscal stability. Mengjin District's GRP has ranked top among all the districts or counties in Luoyang City for years.

Henan Province is a leading economic province and is recognized as one of the most developed provinces in China. It is located at the junction of the three major regions in China, including eastern, central and western regions. It has a strategic position as an important transportation and communication hub, and a material distribution center in China. With the good transportation and location advantages, Henan Province's GRP ranked 6<sup>th</sup> among all provinces in China in 2023 with a GRP of RMB5.9 trillion and growth rate of 4.1% year-on-year ("YoY"). Meanwhile, its general budgetary revenue increased by 6.2% YoY to RMB451.2 billion. In the first half of 2024, Henan Province achieved a GRP of RMB3.1 trillion, representing a YoY increase of 4.9%.

Luoyang City is located in the west of Henan Province, which is the sub-central city in the Central Plains Urban Agglomeration. It is one of the first batch of historical and cultural cities announced by the State Council, and is also an important industrial city in the central region in China. Luoyang City is also an important transportation hub in the central and western regions of China with several rail networks. Supported by its location advantages, Luoyang City has developed five pillar industries, namely advanced equipment manufacturing, new materials, high-end petrochemicals, electronic information, as well as tourism industries. Luoyang City demonstrated ongoing economic growth over the past three years, with GRP ranked 2<sup>nd</sup> among 18 prefecture-level cities in Henan Province. In 2023, it reported a GRP of RMB548.2 billion, representing a YoY growth of 3.5%. In the first half of 2024, Luoyang City's GRP was RMB289.0 billion, contributing about 9.3% of Henan's total GRP. The Luoyang Municipal Government's general budgetary revenue also increased to RMB40.4 billion from RMB39.8

billion in 2021. Tax accounted for over 60% of its general budgetary revenue over the past three years, indicating a relatively good fiscal quality. Meanwhile, Luoyang Municipal Government's fiscal sufficiency was moderate, with the fiscal balance ratio (general budgetary revenue/general budgetary expenditure) averaging 62.0% over the past three years. As of end-2023, its government debt balance amounted to RMB120.3 billion, accounting for 21.9% of GRP.

### Exhibit 3. Key economic and fiscal indicators of Luoyang City

	2021FY	2022FY	2023FY
GRP (RMB billion)	544.7	567.5	548.2
GRP Growth (%)	4.8	3.0	3.5
General Budgetary Revenue (RMB billion)	39.8	39.8	40.4
General Budgetary Expenditure (RMB billion)	64.2	62.9	66.7
Local Government Debt (RMB billion)	63.0	77.5	120.3

Source: Luoyang Municipal Government, CCXAP research

Mengjin District is located in the northwest region of Henan Province, which is under the jurisdiction of Luoyang City. After years of development, Mengjin District has formed three pillar industries, including high-end petrochemicals, advanced equipment manufacturing, and special new materials. It also developed four major industrial parks, namely Luoyang Circular Economic Park, Luobei Modern Service Industry Cluster, Xincheng Science and Technology Park, and Dry Port Modern Logistics Park. In 2023, Mengjin District's GRP amounted to RMB50.4 billion, ranking 4<sup>th</sup> among all the districts or counties in Luoyang City. During the first six months of 2024, Mengjin District achieved a GRP of RMB28.0 billion, with a YoY growth rate of 10.8%, ranking 1<sup>st</sup> among all the districts or counties in Luoyang City in terms of growth rate. In 2023, its general budgetary revenue increased to RMB4.2 billion, of which tax revenue accounted for 60.0% of its general budgetary revenue. In addition, Mengjin District Government has good self-sufficiency, with its fiscal balance ratio averaging 85.8% over the past three years. As of 31 December 2023, the outstanding debt of Mengjin District Government was RMB5.4 billion, accounting for 10.6% of its GRP.

### Exhibit 4. Key economic and fiscal indicators of Mengjin District

	2021FY	2022FY	2023FY
GRP (RMB billion)	55.4	54.2	50.4
GRP Growth (%)	4.8	-0.6	0.6
General Budgetary Revenue (RMB billion)	3.2	4.2	4.2
General Budgetary Expenditure (RMB billion)	4.5	4.3	4.7
Local Government Debt (RMB billion)	3.7	4.3	5.3

Source: Mengjin District Government, CCXAP research

## Government's Willingness to Provide Support

### Important role in infrastructure construction and urban operation of Mengjin District

There are mainly four LIIFCs in Mengjin District under the control of the local government, of which LYGX and Luoyang Shengshi City Construction Investment Co., Ltd. ("LYSS") are the major LIIFCs. LYGX is the largest LIIFC by assets in Mengjin District, focusing on infrastructure construction and public utility operation in Mengjin District. LYGX holds 49.0% shares in LYSS, who is mainly responsible for the resettlement housing and ecological-related infrastructure construction such as sewage treatment and river regulation.

Entrusted by the local government or local state-owned enterprises, LYGX undertakes infrastructure construction through agency construction model. The Company signed construction agreements with the entrusting parties and would 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 31 December 2023, LYGX had completed several infrastructure construction projects, mainly including road construction and shantytown projects, with a total investment of RMB3.1 billion. The Company also had 7 infrastructure construction projects under construction as of the same date, with a total investment amount of RMB4.9 billion and an uninvested amount of RMB1.4 billion. Meanwhile, the Company had an infrastructure construction project under planning, requiring a total estimated investment of RMB400 million.

Moreover, LYGX provides water supply services in Mengjin District with strong competitiveness, covering the entire Mengjin District (including urban areas and townships). As of end-2023, the Company had 3 water supply plants and 9 township water supply centers with a daily water supply capacity of 145 thousand tons. The profitability of water supply businesses is relatively weak due to its social welfare nature and the price is relatively low. The local government has provided subsidies to support its operations. LYGX also had 2 water plants constructed waiting to be put into operation, the daily water supply capacity is expected to increase by 3 thousand tons. The Company is also responsible for sewage treatment in Mengjin District, with a service area of 14 square kilometers and a daily sewage treatment capacity of 20,000 tons. Considering the Company's important role in infrastructure construction and urban operation of Mengjin District, we believe that the Company will not be easily replaced by other local state-owned enterprises in the foreseeable future.

### **Increasing exposure to commercial activities**

In addition to public activities, LYGX participates in various commercial activities, including self-operated construction and engineering construction. The Company is also expanding its business scope to mining and sales of sand and gravel business as well as tourism operation. While these commercial activities generate supplemental income, they may also pose higher operational and business risks than its public-policy businesses. Considering the Company's ongoing investment in these projects, we believe that LYGX's exposure to commercial activities will increase in the future.

Apart from public policy projects, LYGX had several self-operated projects under construction and planning, which may increase its future investment pressure. The Company undertakes self-operated construction projects with self-raised funds and is expected to achieve funding balance through future operating income such as rental income, ticket sales and parking fees. As of 31 December 2023, the Company had one self-operated project under construction with invested amount of RMB585 million. There were also 6 self-operated projects under planning, with a total investment of RMB3.0 billion as of the same date, such as industrial parks and hotel projects. The large investment needs in self-operated projects will bring certain capital expenditure pressure to the Company. In addition, there are uncertainties in the future operation of self-operated projects, and the payback cycle might be long.

Furthermore, LYGX undertakes engineering construction business, mainly the construction of water pipeline for households in the community, including the upgrading, renovating and expanding of water supply infrastructure in Mengjin District. Apart from the water pipeline projects, the Company also had one ethylene-supporting land leveling project under construction with a total contracted amount of RMB405 million. From 2021 to 2023, the revenue from engineering construction business increased from RMB23.3 million to RMB116.0 million.

Apart from that, LYGX generates supplementary income through management and operation of underground pipelines, including water and heat pipe network. The Company generates income through leasing of the

pipelines to local water supply, sewage treatment, and heating supply companies and collects rental payment at the end of each year. The underground pipe network contributed around RMB42.4 million to the Company's total revenue annually from 2021 to 2023.

In addition, LYGX possesses high-quality tourism resources in Mengjin District. Along with the equity transfer of Mengjin Hanwei Tourism Resources Development Group Co., Ltd. in December 2023, the Company started to engage in tourism business by operating one 4-A level scenic spot and three 3-A level scenic spots. In the first half of 2024, this segment generated revenue of RMB12.9 million to the Company, mainly from ticket sales and tourism service. With the recovery of tourism industry, we expect the tourism business to provide supplementary income to the Company in the future.

### **Good track record of receiving government support**

LYGX has a good track record of receiving support from the local government in the form of equity and asset transfers, capital injections, and operating subsidies to support its investments and the operation of its businesses. Since its establishment, the local government transferred equity shares of several state-owned enterprises in Mengjin District to the Company, such as 100% shares of Mengjin County Water Investment Development Co., Ltd. Thereby, the Company acquired assets without compensation, including water supply plants, water and heat pipe networks, land use rights, and infrastructure construction projects. In 2023, the local government further injected a 30-year income rights of sand and gravel resources into the Company. The equity and asset transfers enhanced the Company's capital strength, increasing its paid-in capital and capital reserve notably by RMB848.2 million and RMB11.6 billion from 2022 to 2024H1.

In addition, LYGX has a track record of receiving government payments. From 2021 to 2024H1, the local government provided subsidies of RMB230.0 million to the Company to support its operation and development. LYGX also received project repayments of around RMB148.3 million from the local government for its infrastructure construction over the same period. Considering its strong policy role in Mengjin District, we expect the local government will continue to provide support to the Company.

### **Increasing debt burden and moderate asset liquidity**

Due to the continuous investment in infrastructure construction projects, LYGX's total debt has been growing moderately over the past three years. As of 30 June 2024, LYGX's total debt increased to RMB3.9 billion from RMB2.8 billion as of end-2021. However, owing to the significant increase in equity resulting from capital injection, the Company's total capitalization ratio, as measured by total debt to total capital, decreased from 36.4% to 17.1% over the same period. As of 30 June 2024, the Company's short-term debt was RMB366.4 million, accounting for 9.3% of total debt, and the cash to short-term debt ratio was 0.2x, which could not fully cover the short-term debt. Considering the ongoing investment in infrastructure and self-operated projects under construction and planning, we estimate that the Company would continue to rely on external financing such as bank loans to support its business, and its debt level would further increase over the next 12-18 months.

LYGX's asset liquidity was moderate. As of 30 June 2024, the Company's receivables, inventories, fixed assets and intangible assets accounted for around 67.5% of the total assets, all of which are considered low liquidity. The Company's inventories mainly include the cost of construction works, while intangible assets are mainly the income rights of sand and gravel resources transferred by local government as well as the land use rights, which are considered low liquidity.

## Fair access to funding channels

LYGX had a high reliance on bank loans for its capital expenditure, of which bank loans accounted for the majority of its total debts. The Company maintains long-term and close relationships with policy banks, large state-owned banks, and state-owned commercial banks, such as Agricultural Development Bank of China and China Construction Bank Corporation. As of 30 June 2024, the Company had obtained total credit facilities of RMB4.3 billion with an unutilized amount of RMB786.0 million. In addition, the Company had a manageable exposure to non-standard product financing, accounting for less than 5% of its total debt as of same date. Due to the capital expenditure pressure from its business plan, the Company is expected to expand the financing channels to debt capital market in the next 12-18 months.

## ESG Considerations

LYGX bears environmental risks through its infrastructure construction projects. Such risks could be mitigated by conducting environmental studies and detailed planning before the commencement of the projects and close supervision during construction.

LYGX bears social risks as it implements public policy initiatives by building public infrastructure and providing water supply service in Mengjin District. 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.

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

## Structural Consideration

LYGX'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 important role in infrastructure construction and urban operation of Mengjin District, 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 \(July 2022\)](#).

## Appendix

### Exhibit 5. Peer comparison

	Luoyang Guoxing Investment Holding Group Co., Ltd.	Luoyang Shengshi City Construction Investment Co., Ltd.
Long-Term Credit Rating	BBB <sub>g</sub>	BBB <sub>g</sub> -
Shareholder	Finance Bureau of Mengjin District (100.0%)	Luoyang City Development Investment Group Co., Ltd. (51.0%) and LYGX (49.0%)



Positioning	Core entity in infrastructure construction and urban operation of Mengjin District	Important entity in resettlement housing and infrastructure construction of Mengjin District
Total Asset (RMB billion)	24.0	19.1
Total Equity (RMB billion)	19.0	9.5
Total Revenue (RMB billion)	1.5	1.0

All ratios and figures are calculated using CCXAP's adjustments based on financial data in 2023.

Source: Company information, CCXAP research



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