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NON-RATING ACTION COMMENTARY

Toll Reduction to Have Limited Impact on Chinese Toll Road Operators

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Fitch Ratings-Singapore/Hong Kong-25 October 2022: Reduced toll rates for trucks in China will have only a limited impact on the rated Chinese toll road operators, Fitch Ratings says. Their credit profiles are more dependent on their capex plans and Covid-19-related restrictions.

The Chinese government said it will reduce truck toll tariffs by 10% across the country in 4Q22. However, truck traffic contributed to 30% of total weighted-average volumes in 2021 for our rated Chinese toll road companies. Hence, we expect the effect to be manageable and short-lived, if any.

Lower toll rates could also provide a boost to volumes, which have been slower to recover than we expected after wider and extended lockdowns in some cities in April to June. The rebound has been hampered by a resurgence of Covid-19 cases and continued containment measures to keep the virus at bay. Toll traffic dropped by up to 10% across all issuers in the first eight months of 2022.

Among the rated entities, Zhejiang Expressway Co., Ltd. (ZJE, A+/Stable, underlying credit profile: bbb+) and Yuexiu Transport Infrastructure Limited (YXT, BBB/Stable) have more resilient credit profiles, supported by larger rating headroom against long periods of weaker revenue. In contrast, a prolonged slump in revenue would have a larger negative impact on Shenzhen Expressway Company Limited (SZE, BBB+/Negative, underlying credit profile: bbb) and Shenzhen International Holdings Limited (SZIH, BBB+/Negative, underlying credit profile: bbb-).

SZE's update on 30 September about its overall construction and financing plan for the Jihe expansion project showed that its near-term capex will be higher than we previously expected. We expect this and the likely reduction in toll revenue on account of pandemic related measures to bring SZE's leverage to close to the negative rating sensitivity over the next two to three years when capex peaks.

SZE’s Issuer Default Rating (IDR) and Outlook are equalised with that of its parent, SZIH. The Negative Outlook on the rating on SZIH reflects Fitch’s expectation that net leverage will remain above our negative trigger in the near term. This is due to aggressive capex plans at both SZE and SZIH, which include expansion of its logistics operations and other non-toll road businesses. Near-term net leverage will also be pushed up by Jihe’s expansion and weaker performance of its logistics parks as a result of a slowdown in China’s economy.

Nevertheless, Fitch view SZIH’s recent efforts to dilute its exposure in the more volatile property sector in China positively, as it will allow SZIH to redirect resources to the development of its core logistics parks businesses in economically developed and high industrial growth regions, where land is becoming increasingly scarce. We believe that SZIH’s cautious approach to selecting locations for its logistics parks will also be positive for its credit profile in the longer term.

YXT recently finalised terms and conditions of its acquisition of Lanwei Expressway, which has been operating for more than 17 years. Simultaneously, YXT also announced finalisation of the land expropriation agreement for the preliminary works for the Guangzhou City Northern Second Ring Expressway expansion project. The broad terms and investment plans are largely in line with Fitch’s expectations.

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