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S&P Global
China Ratings

Unsolicited Rating Report:

Shaanxi Coal and Chemical Industry Group Co., Ltd.

Issuer Credit Rating*: $A_{spc(u)}$; Outlook: Stable

February 18, 2022

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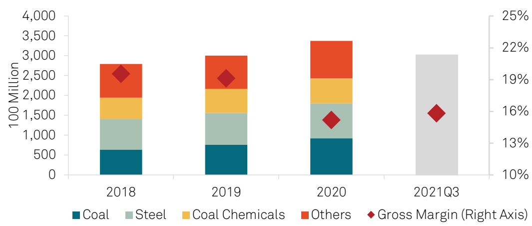
Tear Sheet

Company Name	Rating Type	Current Rating	Rating Date	Outlook/CreditWatch
Shaanxi Coal and Chemical Industry Group Co., Ltd.	Issuer Credit Rating	$A_{spc(u)}$	February 18, 2022	Stable

Industry Classification: Mining.

Company Profile: Shaanxi Coal and Chemical Industry Group Co., Ltd. ("Shaanxi Coal and Chemical Group" or "company") is an SOE under the Shaanxi Province State-owned Assets Supervision and Administration Commission (SASAC). Headquartered in Xi'an, Shaanxi, it was established in 2004 with registered capital of 10 billion RMB. The company was formerly known as Shaanxi Coal Industry Group Co., Ltd. After several reorganizations and asset transfers, the company has formed several business segments including coal mining, coal chemicals, steel production, machinery manufacturing, construction, logistics and trade. Shaanxi SASAC holds 100% of the company and is its actual controller. By the end of September 2021, total assets were 638.3 billion RMB and shareholders' equity (including minority shareholders' equity) were 198.6 billion RMB. In the first three quarters, total revenue was 304.7 billion RMB, up 26.9% YoY. Net profit was 12.6 billion RMB.

2018-2021Q3 Revenue Composition



Note: The company did not disclose its revenue composition as of the end of the third quarter of 2021.
Source: Wind, S&P Global (China) Ratings.

Economy and Industry Trends: We expect China GDP growth to be 4.9% in 2022. The ongoing economic recovery in China and overseas should see demand for thermal coal remain healthy in 2022, but weakening steel trading conditions would dampen demand for coking coal. Measures in place to guarantee supplies and release production from modern capacity should lift coal supply, but we expect the government to maintain control over total coal output. Raw coal production is expected to increase by about 3% to 5% in 2022. Coal prices could drop with increasing supply, but long-term contract prices are set to remain high. This could maintain benign profits for coal producers, helping them to improve their credit quality.

Credit Highlights: The rating reflects our view of the company's abundant coal reserve, enormous production scale and ability to maintain sustainable business development. Production costs are low thanks to its scale advantages, good geographical condition, modern equipment and good operating efficiency. However, the cyclical nature of the industry can lead to product price volatility. It has large-scale debt and high leverage. The company also faces significant subordination risks as debt is mainly incurred at the parent company level while cash flows are generated by its coal operating subsidiary. The Shaanxi government has very strong support capacity, and we believe the company is of critical importance to the Shaanxi government.

Key Metrics:

	2020A	2021E	2022F
EBITDA margin (%)	12.1	12-15	11.5-14.5
Debt/EBITDA (x)	7.7	5-6	6-7
EBITDA interest coverage (x)	2.6	3-4	2.5-3.5

Note: Above data adjusted by S&P Global (China) Ratings. A-actual, E-estimated, F-forecast.

Rating Snapshot:

Issuer Credit Rating:	$A_{spc(u)}$/Stable
Business Risk Profile:	3/Satisfactory
Industry Risk:	4/Moderately high
Competitive Position:	2/Strong
Financial Risk Profile:	5/Aggressive
Anchor:	bb+
Adjustments	
Diversification:	Neutral (no impact)
Capital Structure:	-1
Financial Policy:	Neutral (no impact)
Liquidity:	Adequate (no impact)
Management & Governance:	Neutral (no impact)
Comparable Ratings Analysis:	Neutral (no impact)
Stand-alone Credit Profile:	$bb_{spc(u)}$
External Influence:	+6

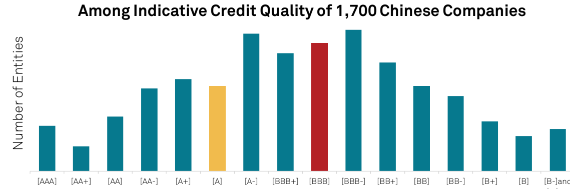
Business Risk Profile: The satisfactory business risk profile reflects its rich coal reserves, enormous production scale at 195 million tonnes in 2020, and ability to maintain sustainable development. Its assets are well diversified with sound geological conditions. The quality of its coal products is good, and full production costs are low at 220-230 RMB per tonne. The company's coal product mix is good, with a stable and broad range of sales. However, the company's location is not advantageous, and operating pressure exists for some of its non-coal businesses. The cyclical nature of the industry can lead to product price volatility.

Financial Risk Profile: We view its financial risk profile as aggressive, reflecting its large-scale debt, unstable operating cash flow and high leverage. 2021's high coal prices are expected to generate strong cash flow, which could help to reduce its leverage, but as coal prices recede in 2022, the company's leverage may return to a high level, due to large capital expenditure associated with several large-scale projects under construction.

Capital Structure: We apply a one-notch downward adjustment to reflect the significant subordination risk between the parent company and its core listed subsidiary.

External Influence: We view Shaanxi government's ability to support its SOE as strong, and we believe the company is of critical importance to the Shaanxi government. The company is the only large-scale coal producer wholly-owned by the provincial government, and plays an important role in ensuring energy supply, local economic development, tax revenue and employment. The company has large asset scale and profit contribution among Shaanxi provincial SOEs, and enjoys significant government support in areas such as resource acquisition and converting debt into equity.

Position of Shaanxi Coal and Chemical Group's Credit Quality Among Indicative Credit Quality of 1,700 Chinese Companies



Note: The red bar represents the median indicative credit quality of top 1700 entities, and the yellow bar represents the position of Shaanxi Coal and Chemical Group.

Peer Comparison

(2019-2020 two-year average, RMB, millions)	Shaanxi Coal & Chemical Group	China Shenhua	Shandong Energy Group	Jinneng Holding
Total revenue	318,993	237,567	675,240	192,607
EBITDA	43,164	86,041	48,641	15,824
Debt/EBITDA (x)	7.1	0.1	6.9	16.2
EBITDA interest coverage (x)	2.7	26.1	3.9	1.7

Note: Above data adjusted by S&P Global (China) Ratings. China Shenhua – China Shenhua Energy Company Limited; Shandong Energy Group – Shandong Energy Group Co., LTD.; Jinneng Holding – Jinneng Hold Coal Industry Group Company Limited. Source: Wind, S&P Global (China) Ratings.

Declaration

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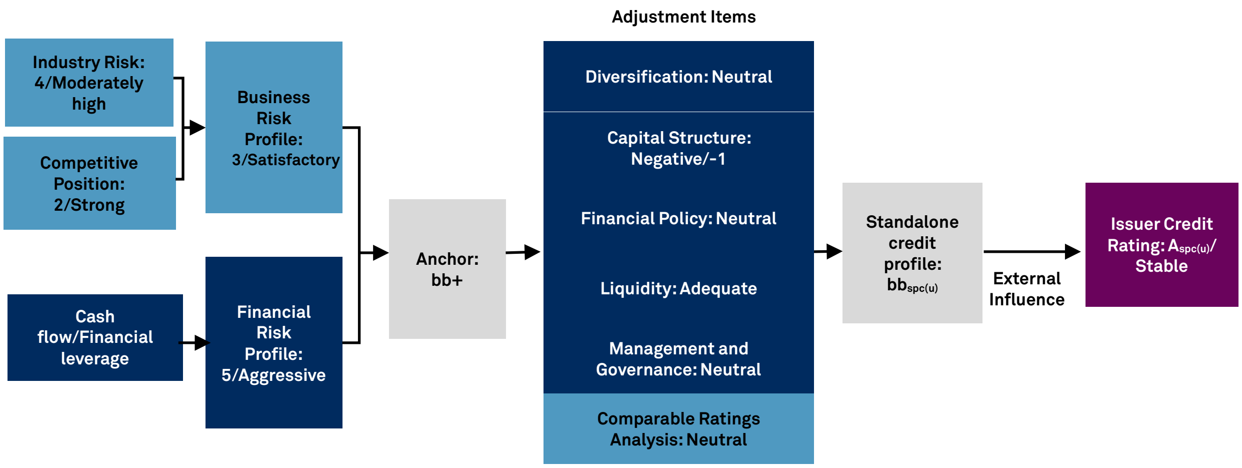
Rating Summary

Company Name	Rating Type	Current Rating	Rating Date	Outlook/CreditWatch
Shaanxi Coal and Chemical Industry Group Co., Ltd.	Issuer Credit Rating	$A_{spc(u)}$	February 18, 2022	Stable



Credit Highlights

Strengths	Weaknesses
The company has abundant coal reserves, outstanding scale advantages and high business sustainability.	The company is in a strongly cyclical industry with high volatility in product prices.
Thanks to its outstanding scale advantage, abundant coal reserves, mechanized equipment and operational efficiency, the company's production cost is low.	The company has large debt with high financial leverage.
The company is of critical importance to the Shaanxi Provincial Government and the credit quality of the company has been greatly improved thanks to support from the government.	There is significant subordination risk between the parent company and its core listed subsidiary.

Outlook

The rating outlook for Shaanxi Coal and Chemical Industry Group Co., Ltd. is stable. In our opinion, the stable outlook reflects our view that the company can maintain its strong competitive position in the coal industry over the next 24 months, with scale remaining at a leading level and costs remaining low. We do not expect the company's financial risk to deteriorate significantly, although changes in coal prices may still expose the company to fluctuations in financial leverage. At the same time, the company is set to remain important to Shaanxi Provincial Government.

Upside scenario: We might consider upgrading the company's issuer credit rating if: 1. The company decreases its financial leverage by a large margin, for a sustained period. This is achieved through reducing its debts and equity financing, or development of its non-coal businesses that leads to a significant improvement in profitability.; 2. The debt and cash flow structural mismatch between the group's parent company and its core listed subsidiary is significantly improved; and 3. The company's business conditions are improved, which may be reflected in a significant decrease in production costs, improved transportation conditions and further increase in competitiveness of its non-coal business.

Downside scenario: We might consider downgrading the company's issuer credit rating if: 1. The company significantly increases its financial leverage for a sustained period, due to the company's business expansion, capital expenditure, acquisition of other entities, or significant deterioration of earnings caused by its non-coal business; or,

2. The company's competitiveness is reduced significantly and its operating conditions deteriorate, which may be reflected by a significant increase in the production costs, a significant decline in the amount of resources available at its main coal mines and insufficient new production capacity; or, 3. The company's importance to the Shaanxi Provincial Government diminishes, which may be reflected by a decline in the government's shareholding or a divestment of the company's important assets.

Assumptions and Forecasts

Assumptions

- China's GDP is expected to grow by 4.9% in 2022.
- The company's revenue grows by 20%-30% in 2021 and decreases by 0%-10% in 2022.
- From 2021 to 2022, the company's selling and administrative expense ratio is 4.5% - 6.5%.
- The company's EBITDA margins are 12%-15% and 11.5%-14.5% in 2021 and 2022, respectively.
- From 2021 to 2022, the company's annual capital expenditure is 25-32 billion RMB.

Forecasts

Key Metrics

	2020A	2021E	2022F
Debt/EBITDA(x)	7.7	5-6	6-7
EBITDA interest coverage (x)	2.6	3-4	2.5-3.5
EBITDA margin (%)	12.1	12-15	11.5-14.5

Note: The above data has been adjusted by S&P Global (China) Ratings. A: Actual; E: Estimated; F: Forecasted.

Adjusted Financial Data and Indicators

Adjusted Financial Data and Indicators (Unit: mil RMB)

	2018A	2019A	2020A	2021.1-9A
Revenue	279,060	300,441	337,546	304,736
EBITDA	43,967	45,584	40,744	- -
Debt	255,939	296,115	312,422	- -
EBITDA margin (%)	15.8	15.2	12.1	- -
EBITDA interest coverage (x)	3.7	2.8	2.6	- -
Debt/EBITDA (x)	5.8	6.5	7.7	- -

Notes: 1. For details of main adjustments to the financial data, see "Key Financial Data Adjustments"; 2. A: Actual;
3. "--" represents data not available.

Related Methodologies and Research

Related methodologies:

- S&P Global (China) Ratings - Corporate Methodology, July 28, 2020.

- S&P Global (China) Ratings Supplemental Methodology - Materials Industry, May 21, 2019.
- S&P Global (China) Ratings - General Considerations on Rating Modifiers and Relative Ranking, May 21, 2019.

Related research:

- Commentary: Understanding S&P Global (China) Rating Corporate Methodology, July 28, 2020.
- Commentary: Understanding S&P Global (China) Ratings General Considerations On Rating Modifiers and Relative Ranking Methodology, June 29, 2020.
- Commentary: Understanding S&P Global (China) Ratings Approach To Support, May 8, 2019.

Economic and Industry Trends

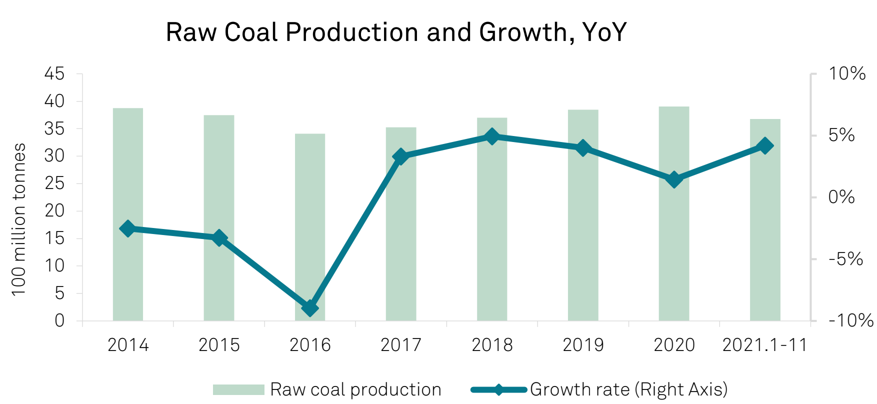
We expect China GDP growth to be 4.9% in 2022. New regulations and policies are aimed at common prosperity and greater self-reliance, marking a shift in China's growth strategy. We have increasingly factored in lower emphasis on the quantity of growth in favor of factors such as deleveraging and lowering inequality so our baseline includes some of these dynamics.

We expect demand for thermal coal to remain at a good level in 2022 as economic conditions in China and overseas continue to recover. However, diminished prospects for the steel industry may suppress demand for coking coal. Production overseas is gradually recovering, and the domestic and international economic recovery, along with efforts to substitute energy sources under China's carbon goals should see solid growth in electricity consumption. This in turn can continue to support demand for thermal power. We expect weakening supply and demand for the steel industry in 2022, with declining industry prospects set to weigh on demand for coking coal.

We expect strong supply assurance measures and the release of advanced production capacity to boost coal supply, with supply and demand possibly returning to an equilibrium in 2022. However, we also believe that the central government will still control the total amount of coal output, and raw coal production may increase by about 3%-5% in 2022. The shortage of coal supplies and high coal prices are one of the main reasons for power shortages seen in 2021. After supply-side reforms and amid China's ongoing carbon goals, total production caps and mining safety protocols remain relatively strict, limiting the growth of output. We expect industry supplies to benefit from the series of measures rolled out to increase production and ensure supply, such as approved increases to production capacity and the signing of long-term agreements. The issue of coal shortages should be gradually alleviated. In our opinion, although upfront capital spending may facilitate the release of coal production capacity in 2022, after supply and demand tightness eases, authorities may remain cautious in their management of coal supplies, and safety measures or efforts to eliminate inefficient production capacity could continue to restrict supply.

With the increase in supply, raw coal production may increase by 3%-5% in 2022, but the central government will still control the total amount of coal.

Chart 1

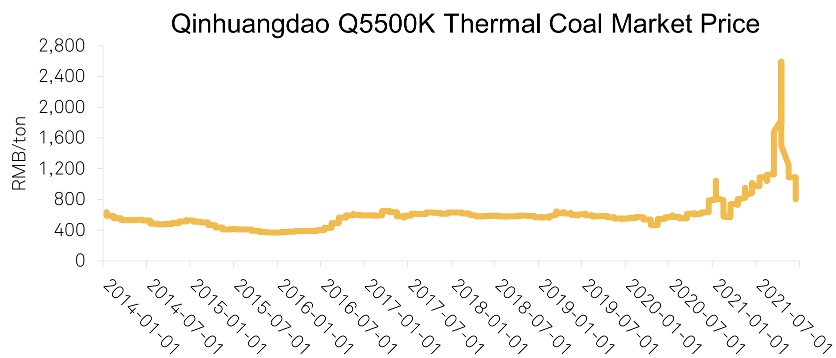


Source: National Bureau of Statistics of China, S&P Global (China) Ratings.

Coal prices should fall but profit margins are still healthy, and the credit quality of some enterprises may improve.

We expect market coal prices to fall with the increase of supply in 2022, but long-term agreement prices should remain high. The National Development and Reform Commission (NDRC) plans to adjust the range of the long-term agreement price to RMB 550- 850/ton. Coal enterprises still have healthy profit margins under the relatively high long-term agreement prices, which is also favorable for the financing environment of coal enterprises and creates conditions for producers to improve their credit quality. However, we also note that financial risk in the sector is generally high, debt scale is high, the deleveraging process is long, and players are very dependent on refinancing. If coal prices fall sharply and the financing environment tightens, the credit quality of some enterprises may deteriorate again. We believe that the credit quality of coal producers that have been proactive in reducing their debts can improve.

Chart 2



Source: Wind, SteelHome, S&P Global (China) Ratings.

Demand from chemical producers may decrease rapidly, with profits set to fall to a reasonable level.

We expect the slowdown of downstream demand growth in 2022 to put pressure on chemical prices. Current high profits should return to more regular levels. In our view, the continuous rise of chemical product prices in 2021 was partly driven by relatively strong downstream demand and partly driven by higher prices of raw materials such as crude oil and coal. We expect China's economic growth to slow down in 2022, and downstream demand may decrease, putting pressure on the prices of some chemicals. We expect China’s carbon goals and environmental policies to lead to a slowdown in growth of fixed asset investment in the chemical industry. Caps on production may significantly limit the supply of chemicals, but supply and demand patterns should be maintained and the likelihood of a significant price fall is low. From a cost perspective, we expect crude oil prices to remain at a relatively high level, which would provide considerable support for prices of petrochemical products. With relatively high oil prices, petrochemical enterprises can maintain relatively good profit margins. Coal prices should be considerably lower than in 2021, making it possible for better profits across the coal chemical industrial chain. On the whole, we expect chemical enterprises’ profits to fall from their current peak. Profits should however remain at a good level, which can help stabilize players’ credit quality.

Falling prices should support profit margins.

In 2022, there may be a significant decline in steel prices compared with 2021, potentially falling to a level just above 4,000 RMB/ton. Meanwhile, iron ore and coking coal prices should also drop significantly. In the first half of 2021, demand for steel was strong, and steel supply and prices increased at the same time. In the second half of the year, demand fell rapidly. Although supply was controlled by various policies, the sharp downward trend of prices was hard to avoid. We estimate that steel may see weak supply and demand patterns in 2022. On the one hand, the growth rate of investment in real estate construction and installation should slow down; and on the other hand, it is difficult to see a significant uptick in demand for infrastructure, automobile, machinery and other industries, leaving demand for steel in a state of weak growth. While environmental policies, China's carbon goals and supply-side reforms may cap crude steel output to no more than 1 billion tonnes, such supply limits would still struggle to keep prices high. As prospects for the steel sector decline, demand for raw materials such as iron ore and coking coal would decrease. In addition, the supply of raw materials should also increase, leading to a significant drop in raw material prices. Where both steel and raw material prices drop, steelmakers still have decent profit margins and cash flow should remain stable.

Anchor

Company Description

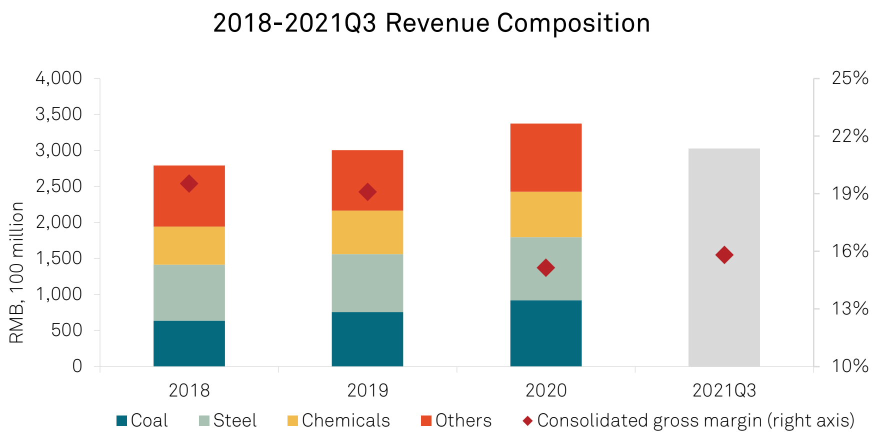
Shaanxi Coal and Chemical Industry Group Co., Ltd. (SCCIG or the company) is a state-owned enterprise (SOE) managed by the State-owned Assets Supervision and Administration Commission of Shaanxi Province (Shaanxi SASAC), which was established in 2004 with registered capital of 10 billion RMB in Xi'an, Shaanxi Province. The company's predecessor was Shaanxi Coal Group Co., Ltd., and it has undergone several reorganizations and asset transfers. It has business lines in coal mining, chemicals, steel smelting, machinery manufacturing, construction, logistics and trading.

As of today, Shaanxi SASAC holds 100% of the equity of SCCIG and is the actual controller of the company. SCCIG's listed subsidiaries are Shaanxi Coal Industry Company Limited, an entity dedicated to coal and engineering machinery (601225.SH, Shaanxi Coal) and Shaanxi Construction Machinery Co., Ltd. (600984.SH). Shaanxi Coal is the main operating entity for the company's coal business and an important profit source for the company. The company also holds equities in listed companies such as Shaanxi International Trust Company Limited (000563.SZ) and Shaanxi Beiyuan Chemical Industry Group Company Limited (601568.SH).

The company's coal segment includes coal mining, washing, transportation, sales and production services, and its coal products are mainly used in power, chemical and metal industries. As of the end of September 2021, the company had coal reserves of 30 billion tonnes, with recoverable reserves of 20.3 billion tonnes and an approved production capacity of 181.15 million tonnes per year. The company's main entity for chemicals is Shaanxi Chemical Industry Co., Ltd. with five industrial departments focused on fertilizers, coking, salinization, coal-based methanol deep processing and coal-to-oil. Its steel business is mainly operated by Shaanxi Iron and Steel Group Company Limited, which has a production capacity of 10 million tonnes for iron, crude steel and steel. The company is also involved in other non-coal businesses such as energy, machinery manufacturing, construction, railroads, and logistics.

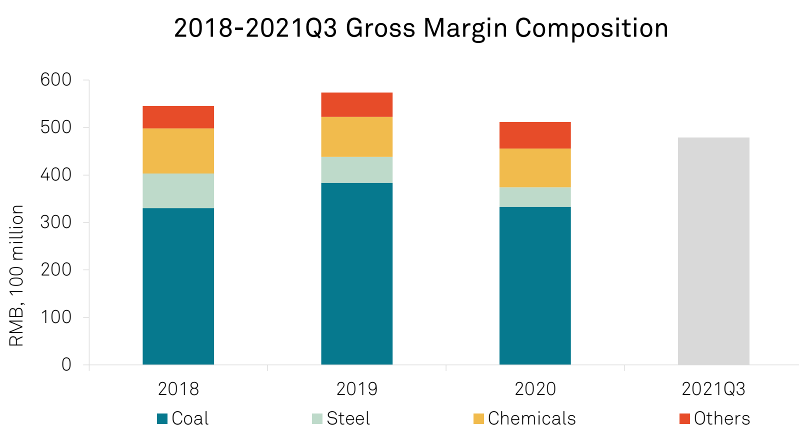
As of the end of the third quarter of 2021, the company had total assets of 638.3 billion RMB, net assets (including minority interests) of 198.6 billion RMB, total revenue of 304.7 billion RMB in the first three quarters, up 26.9% year-on-year, and net profits of 12.6 billion RMB. The composition of the company's revenue and gross profit for 2018-2021Q3 is shown in the following chart:

Chart 3



Note: The company did not disclose the composition of the operating income segment in the third quarter of 2021.
Source: Wind, S&P Global (China) Ratings.

Chart 4



Note: The company did not disclose the composition of the gross profit segment in the third quarter of 2021.
Source: Wind, S&P Global (China) Ratings.

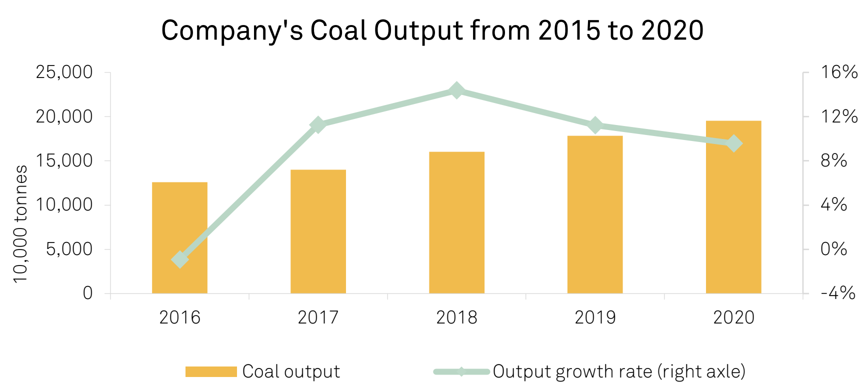
Business Risk Profile

The company has outstanding scale advantages, high business sustainability and low production cost. However, it lacks location advantage, and some of its non-coal interests face some operating pressure.

The satisfactory business risk profile reflects its rich coal reserves, enormous production scale, and ability to maintain sustainable development. Its assets are well diversified with sound geological conditions. The quality of its coal products is good, and full production costs are low. The company's coal product mix is good, with a stable and broad range of sales. However, the company's location is not advantageous, and operating pressure exists for some of its non-coal businesses. The cyclical nature of the industry can lead to product price volatility.

We believe that the company has abundant coal reserves with rising output in recent years, and the business has strong capacity for sustainable development. As of the end of September 2021, the company had 30 billion tonnes of coal reserves and 20.3 billion tonnes of recoverable reserves, with the absolute scale of recoverable reserves ranking among the top in China. At the same time, Shaanxi Provincial Government has clearly identified the company as the sole entity for development of the high-quality coal production base in Shenfunan area, where coal resource reserves are estimated at 30-40 billion tonnes. We expect that with the gradual development of the Shenfunan area, the company's coal reserves may further increase, supporting its long-term development.

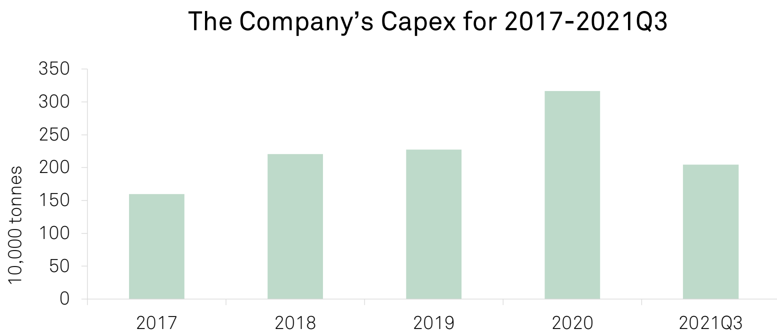
Chart 5



Source: Wind, website of the company, S&P Global (China) Ratings.

However, we also found that some of the company's old mines have been exploited for a long time and are more difficult to mine, and its subsidiaries, such as Tongchuan Mining Bureau, Hancheng Mining, Pubai Mining and Chenghe Mining, all had negative net profits in 2020, impacting on the company's operations. However, the company currently has sufficient resources under construction and in reserve, and we believe that the release of advanced capacity should effectively alleviate the aforementioned pressure. In recent years, the company has shifted its development focus to new areas in northern Shaanxi, where development conditions are better, and it continues to maintain strong capital expenditure. We expect the company's scale advantage to improve as the coal mines under construction are gradually put into operation, increasing its production capacity.

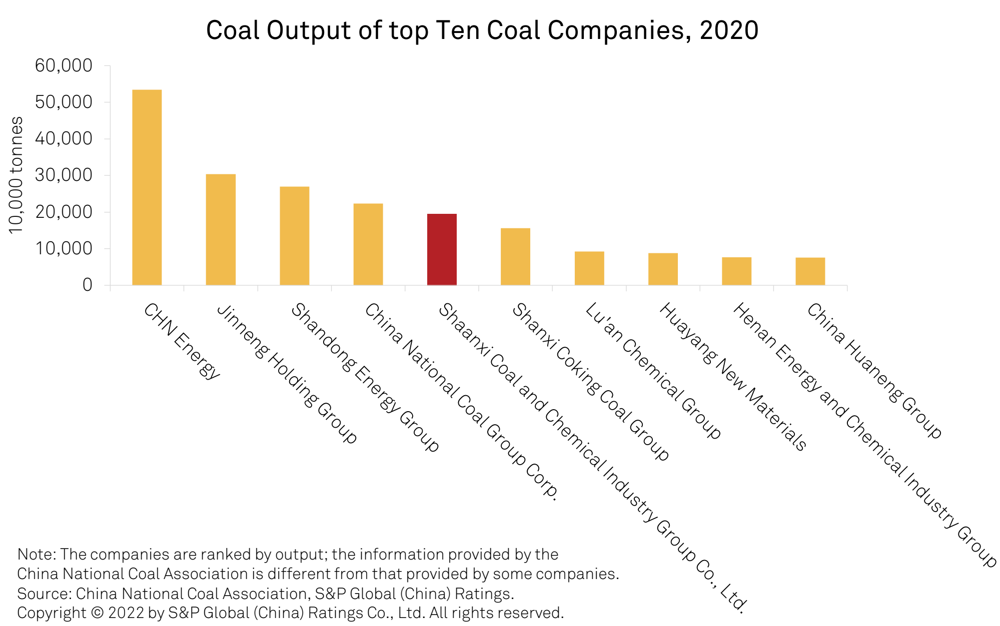
Chart 6



Source: Wind, S&P Global (China) Ratings.

In our opinion, the company has outstanding scale advantages, ranking top in coal production capacity and output in China, and it also has good asset diversification. At the same time, the company's main mines have large individual production capacities, which is conducive to its scale effect. The company is one of six coal companies in the country with output of over 100 million tonnes. As of the end of the third quarter of 2021, the company's coal production capacity was 181 million tonnes per year, with output of 160 million tonnes, 178 million tonnes and 195 million tonnes from 2018 to 2020, respectively. The company ranked fifth in the industry in terms of coal output in 2020 and had 33 wholly owned and controlled mines under production. In terms of single-unit scale, the company also performs well in the industry. At present, a cluster of large-scale mines has been formed in the northern Shaanxi mining area, with five pairs of 10-million-ton mines, namely Hongliulin, Zhangjiashang, Ningtiaota, Xiaobodang No. 1 and Xiaobodang No. 2 (under construction), which, as of large single-unit mines, all help to bring the company's scale advantages into play.

Chart 7



Note: The companies are ranked by output; the information provided by the China National Coal Association is different from that provided by some companies.
Source: China National Coal Association, S&P Global (China) Ratings.

The company has a wide variety of coal products with good quality and a high percentage of long term agreements.

We believe that the company's coal variety is relatively abundant, the coal quality is excellent, and the high proportion of long term coal sale agreements also helps to mitigate against the impact of coal price fluctuations on its revenue and earnings. The company's coal products are mainly high-quality thermal coal, chemical coal and metallurgical coal.

In our opinion, thanks to its outstanding scale advantages, good coal reserves, mechanized equipment and operating efficiency, the company's production cost is low. We believe that for coal producers, operating efficiency and production costs are among the most important factors, due to the industry's high product homogeneity and the fact that product prices are usually very cyclical. The company's complete production cost per ton of coal for 2018-2020 was 216 RMB, 226 RMB and 227 RMB, respectively, which is a low level for the industry. The company has sound coal geological conditions, with the coal seam in the main mining regions at between 200-700 meters. Mining difficulty is low, there is a high degree of mechanization, and safety conditions of production are relatively stable. In recent years, the company's capacity utilization rate has remained high, which is conducive to the reduction of unit costs. At the same time, the company's social burden has been gradually reduced, and historical and personnel burden is moderate. We estimate that the company's production costs would rise in 2021 due to increased spending on safety and environmental protection, but the company may be able to reduce its production costs in the future as advanced production capacity enters a more stable phase.

The company has stable sales channels and a wide sales range, but its location advantage and transportation conditions are not very prominent.

We believe that the company has stable sales channels and a wide sales range. The coal products of the company are mainly sold to Shaanxi Province, central China, southwest China, east China and the southeast coastal region, with a wide sales range. It has established a stable customer group with clients in power, metals and chemical industries inside and outside Shaanxi Province. In 2020, the company's sales from its top five clients totaled 3.9 billion RMB, accounting for 5.3% of its coal business revenue, representing good diversification.

We have also found that the company lacks a prominent location advantage, but its transportation conditions may be improved with the improvement of transportation capacity from the Haolebaoji-Ji'an Railway. Shaanxi is limited by its geographical location, the outbound transportation of coal is limited by the lack of railroad capacity and high transport costs. At present, there is still a shortage of railroad transportation capacity inside and outside the province, and road transportation accounts for a high percentage for the company. We believe that with the release of capacity from the Haolebaoji-Ji'an Railway under the new strategy of "Transporting Coal from North to South China", the company may further improve its capacity for transporting coal to south China to connect to Hubei, Hunan and Jiangxi, provinces with significant coal demand. This would improve the company's current transportation links to some extent.

In our view, the company has established a relatively complete coal-related industry chain, and its chemical, steel and logistics businesses have certain scale advantages in the region and can create synergy with the coal business. However, some of these non-coal businesses are under certain operating pressure. The company's steel products have average added value and are produced at a large scale in the region, with crude steel output of more than 13 million tonnes in 2020. The company's chemical business can rely to some extent on the cost advantage of coal, but the market for methanol, chlor-alkali, urea and other products is oversupplied. In recent years, the gross margin of the company's chemical segment has fallen, and gross profit has gradually decreased. We expect that with the release of capacity from several large domestic refining projects, the company may face poor supply and demand prospects for products from its key investment in the Yulin Chemical Project. The company's logistics business is carried out on a large scale, but its profitability is low, which has a certain negative impact on the company's operation.

Financial Risk Profile

The company has large debt, volatile operating cash flow and high financial leverage, and is expected to maintain high capital expenditure in the future.

We view the company's financial risk profile as aggressive, which reflects its large debt, volatile operating cash flow and high level of financial leverage. We expect that high coal prices may significantly improve the company's cash flow in 2021 and bring down its financial leverage, but with the gradual fall in coal prices, the company's leverage level would become high again in 2022. The company has large projects under construction, and we expect it to maintain high capital expenditure in the future, and debt scale is expected to remain large.

We expect that the company's revenue to rise sharply in 2021, driven by high coal prices and increased trading business; however, with the implementation of policies to ensure supplies and the increase of coal output, coal prices should fall in 2022, and the company's revenue may decline in 2022. However, the higher long-term agreement price is still expected to provide the company with good profit space. We expect that the company's EBITDA margin to rise slightly in 2021 driven by high coal prices, but it should decline in 2022 as coal prices fall back. That being said, EBITDA should still be better than in 2020.

We expect that the company would still maintain high capital expenditure in 2021-2022, with annual investment of 25-32 billion RMB. The company has large projects under construction with investment focusing on new coal mines, the coal chemical industry and other fields, including the Coal Chemical Industry Project for Coal Separation and Utilization in Yulin, which has a huge total investment, and has been resumed again after initially being suspended in the early stages of development. At present, the first phase for the 1.8 million-ton ethylene glycol project with a total investment of over 26 billion RMB is under construction. We expect that the company would continue to maintain strong coal mine construction and development efforts and increase investment in the coal chemical industry to meet its future development goals, and its debt is expected to remain at a high level.

In recent years, the proportion of long-term debt in the company’s total debt has increased and the company has actively promoted debt-to-equity conversion to improve its overall debt structure. As of the end of the third quarter of 2021, the company's long-term debt ratio exceeded 65%, which is at a high level in the industry. As of the end of the third quarter of 2021, the company had unused credit facilities of 196.1 billion RMB, which are sufficient. Since 2017, the company has been actively promoting debt-to-equity conversion, and as of the end of 2020, the company has implemented debt-to-equity conversions with various financial institutions for a total of 51.4 billion RMB, which has improved its debt structure and burden to a certain extent. The company also holds some liquid equity-type assets through its long-term equity investments, which also have a positive effect on mitigating its financial risk.

Table 1

Adjusted Key Financial Data and Indicators of the company (Unit: mil RMB)					
	2018A	2019A	2020A	2021E	2022F
Revenue	279,060	300,441	337,546	Year-over-year revenue growth in 2021: 20%-30%; capital expenditure 25-32 billion RMB. Year-over-year revenue reduction in 2022: 0%-10%; capital expenditure 25-32 billion RMB.	
EBITDA	43,967	45,584	40,744		
CFO	27,732	25,185	19,770		
Interest Expenditure	11,890	16,466	15,869		
Capital Expenditure	22,071	22,734	31,663		
Debt	255,939	296,115	312,422		
Owner's Equity	135,450	139,303	154,292		
Adjusted Core Financial Indicators					
EBITDA margin (%)	15.8	15.2	12.1	12-15	11.5-14.5
Debt/EBITDA(x)	5.8	6.5	7.7	5-6	6-7
EBITDA interest coverage (x)	3.7	2.8	2.6	3-4	2.5-3.5

Note: A: Actual; E: Estimated; F: Forecasted.

Source: Wind, S&P Global (China) Ratings.

Table 2

Financial Data Adjustments of the company - as of December 31, 2020 (Unit: mil RMB)					
	Total Debt	Equity attributable to owners of the parent company (excluding perpetual debt)	EBITDA	Interest Expenditure	EBITDA
Reported Value	303,548	28,445	38,329	12,650	38,329
Adjustment by S&P Global (China) Ratings					
Interest Expenditure	-	-	-	-	-12,650
Interest and dividend income	-	-	-	-	1,029
Current income tax	-	-	-	-	-6,134
Surplus cash	-33,034	-	-	-	-
Capitalized interest	-	-	-	3,219	-3,219
Disposal costs	8,188	-	-	-	-
Perpetual debt	30,646	-	-	-	-
Cash dividends from long-term equity investment	-	-	1,653	-	1,653
External guarantee	3,074	-	-	-	-
Minority interests	-	125,847	-	-	-
Others	-	-	762	-	762
Total adjustment	8,875	125,847	2,415	3,219	-18,559
S&P Global (China) Ratings' adjusted amounts					
	Adjusted total debt	Owner's Equity	EBITDA	Interest Expense	FFO

After adjustment	312,422	154,292	40,744	15,869	19,770

Note: Total debt = long-term debt + short-term debt.
Source: Wind, S&P Global (China) Ratings.

Peer Comparison

We have selected China Shenhua Energy Company Limited (China Shenhua), Shandong Energy Group Co., Ltd. (Shandong Energy Group) and Jinneng Holding Coal Group Co., Ltd. (Jinneng Coal) as peer companies, since they are all large-scale coal production and sales enterprises in China.

We believe that SCCIG and its peers have relatively strong competitive advantages. In terms of resource reserves, the peer companies have abundant recoverable coal reserves, which can better support their sustainable development. The absolute size of the company's recoverable reserves is outstanding in the industry, and it is the only entity designated by the Shaanxi Provincial Government to mine in Shenfunan area. However, compared to the peer group, the company has less of a location advantage and a lower share of low-cost rail transportation. China Shenhua is the second largest railroad operator in China with excellent transportation capacity by rail and water; Jinneng Coal's main production bases are close to coal transportation corridors and linked to coal ports; Shandong Energy Group has good location advantages and its main production areas are close to east China, north China and other regions with high demand for coal.

In terms of scale, these comparable enterprises are all in leading positions in China, with a coal production capacity of over 100 million tonnes. SCCIG and China Shenhua are more prominent in terms of the size of their individual mines, with China Shenhua having several 20-million-ton coal mines and the company having several 10-million-ton mines in the northern Shaanxi region, with advanced capacity gradually being released. In terms of regional distribution, the mines of the company and Jinneng Coal are concentrated in a single province, while the mines of other companies are spread over a relatively wide area, which can mitigate against impacts from regional policy changes etc.

We believe that SCCIG and China Shenhua have higher operating efficiency and cost control capabilities, while Jinneng Coal has a lower operating efficiency due to its heavy historical and personnel burden and the age of some of its coal mines. In terms of production cost, both SCCIG and China Shenhua are at a low level in the industry, with China Shenhua's cost advantage being more prominent. Jinneng Coal has a heavy personnel burden, low gross margin in its coal business, and high sales and management expense ratio.

In terms of financial risk, China Shenhua has the lowest financial leverage among the peer group thanks to its excellent profitability. SCCIG and Shandong Energy Group have a higher debt burden and financial risk, and Jinneng Coal has a poor debt structure, the heaviest debt burden and higher maturity pressure in the coming year.

Table 3

Peer Business Profile				
2020	SCCIG	China Shenhua	Shandong Energy Group	Jinneng Coal
Enterprise nature	Local SOE	Central SOE	Local SOE	Local SOE
Total assets (100 mil RMB)	5,961	5,584	6,851	3,888
Recoverable reserves (100 million tonnes)	203	144	208	1631
Coal production capacity (100 million tonnes)	1.81	3.40	3.50	1.51
Coal output (100 million tonnes)	1.95	2.92	2.70	1.74

Note: 1. The recoverable reserves of Jinneng Coal are as of the end of September 2020.

Source: Wind, public information, S&P Global (China) Ratings.

Table 4

Peer Adjusted Financial Position (2019-2020 two-year average, unit: mil RMB)				
	SCCIG	China Shenhua	Shandong Energy Group	Jinneng Coal
Revenue	318,993	237,567	675,240	192,607
EBITDA	43,164	86,041	48,641	15,824
EBITDA margin (%)	13.6	36.2	7.2	8.2
Debt/EBITDA(x)	7.1	0.1	6.9	16.2
EBITDA interest coverage (x)	2.7	26.1	3.9	1.7

Note: The data of Shandong Energy Group in 2020 is shown.

Source: Wind, S&P Global (China) Ratings.

Stand-Alone Credit Profile

Liquidity

In our view, the company has adequate liquidity. We expect the company to be able to cover its liquidity needs with a multiple of 1.2x from its liquidity sources in the coming year.

The company has adequate liquidity.

Table 5

Liquidity Source	Liquidity Use
Over the next 12 months, the company should have cash and cash equivalents on hand, net cash flow from operations, and liquidity funds through various channels totaling 190-200 billion RMB.	Over the next 12 months, the company's cash outflows for debt repayment, net working capital outflows, and capital expenditure should total 160-170 billion RMB.

Note: As of the end of the third quarter of 2021.

Source: Wind, S&P Global (China) Ratings.

Table 6

Distribution of debt principal maturity

Period	Amount (unit: mil RMB)
Within one year	114,121
Over one year	236,438
Total	350,559

Note: As of the end of the third quarter of 2021. The principal of the debt includes short-term borrowings, notes payable, non-current liabilities due within one year, long-term borrowings, bonds payable, lease liabilities and perpetual debt.

Source: Wind, S&P Global (China) Ratings.

Capital Structure

We apply a one-notch downward adjustment for capital structure, to reflect the large debt and cash flow structural mismatch between SCCIG and its core listed subsidiary Shaanxi Coal. If SCCIG's refinancing channels are restricted, it may face greater pressure to pay off its debt. We note that Shaanxi Coal is the main source of the company's profit and cash flow. However, Shaanxi Coal has a low level of debt, with most of its debt held at the parent level. Meanwhile, the independence of the listed company further increases SCCIG's cash flow and debt structural mismatch, and SCCIG is highly reliant on refinancing. We believe that this mismatch increases SCCIG's financial and refinancing risks.

Issuer Credit Rating

SCCIG is the largest coal enterprise group under the Shaanxi SASAC, and the Shaanxi government has strong ability to support the SOEs under its jurisdiction. We believe that the company is of "critical" importance to the Shaanxi government for the following reasons:

- Shaanxi SASAC directly holds 100% of the company's equity and can impose a material influence on the company by assigning directors, supervisors, and senior management. We do not think that the Shaanxi government will reduce its holding in the company in the next 1-2 years.
- Coal is an important pillar industry in Shaanxi, and the company is the only large provincial-level coal enterprise in the province. It supplies energy to the region and plays an important role in local economic development, taxation, and employment.

— The company is an integrator of coal resources and industry chain-related businesses in Shaanxi, with outstanding asset scale and profit contribution among SOEs in the province.

— The company enjoys significant government support in terms of resource acquisition and debt conversion. The company is clearly designated by the Shaanxi government as the sole entity responsible for development of the Shenfunan area in Ordos Basin, and enjoys priority mining rights over some coal mines. In recent years, the company has completed debt-to-equity conversions of over 50 billion RMB under the guidance of the provincial government and has improved its capital structure to some extent.

In summary, our final issuer credit rating on SCCIG is $A_{spc(u)}$.

Rating Score Snapshot

Issuer Credit Rating: $A_{spc(u)}$/ Stable

Business Risk Profile: 3/Satisfactory

Industry Risk: 4/Moderately high

Competitive Position: 2/Strong

Financial Risk Profile: 5/Aggressive

Anchor: bb+

Adjustments

Diversification: Neutral (no impact)

Capital Structure: Negative (-1)

Financial Policy: Neutral (no impact)

Liquidity: Moderate (no impact)

Management and Governance: Neutral (no impact)

Comparable Ratings Analysis: Neutral (no impact)

Stand-alone Credit Profile: $bb_{spc(u)}$

External Influences: +6

Appendix

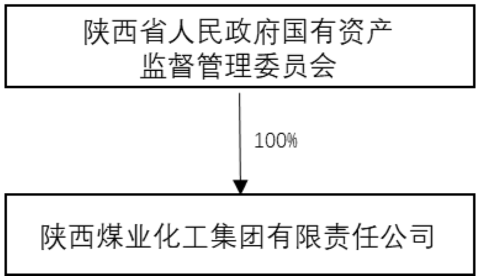
Appendix 1： Main Financial Data and Indicators

Rated Entity's Key Financial Data and Indicators (Unit: mil RMB)	2018	2019	2020	2021.1–9
Monetary cash and trading financial assets	46,864	64,945	75,928	103,541
Fixed assets	168,513	173,499	196,473	188,652
Total assets	500,783	548,595	596,060	638,348
Short-term borrowings	57,172	42,478	46,417	52,930
Notes payable	19,862	18,396	17,924	18,205
Non-current liabilities due within one year	21,038	50,923	50,687	37,986
Long-term borrowings	119,683	103,976	110,917	128,731
Bonds payable	49,293	62,497	70,390	75,638
Total shareholder's equity	135,450	165,761	184,938	198,571
Total revenue	280,587	302,575	340,270	304,736
Operating costs	224,518	243,052	286,367	254,791
Selling expenses	6,038	6,628	4,245	2,019
Administrative expenses	14,521	15,265	15,828	13,780
Financial expenses	11,076	13,486	12,886	10,699
Total profit	13,882	15,695	17,499	16,711
Net profit	10,124	11,708	12,744	12,610
Subtotal of cash inflow from operating activities	269,147	296,911	336,156	283,067
Subtotal of cash outflow from operating activities	232,479	264,095	303,815	254,759
Net cash flow from operating activities	36,668	32,816	32,340	28,308
Subtotal of cash inflow from investing activities	10,542	10,658	36,773	19,304
Subtotal of cash outflow from investing activities	45,035	39,651	70,291	32,704
Net cash flow from investing activities	-34,492	-28,993	-33,518	-13,400
Subtotal of cash inflow from financing activities	179,227	179,115	163,840	137,280
Subtotal of cash outflow from financing activities	177,650	171,185	166,048	125,577
Net cash flow from financing activities	1,577	7,930	-2,208	11,703
Adjusted Financial Data and Indicators				
Debt	255939	296115	312422	--
EBITDA	43967	45584	40744	--
EBITDA margin (%)	15.8	15.2	12.1	--
EBITDA interest coverage (x)	3.7	2.8	2.6	--
Debt/EBITDA (x)	5.8	6.5	7.7	--

Notes: 1. The financial data in the above table are based on the 2018 audit report of SCCIG audited by Xigema Certified Public Accountant (special ordinary partnership) with standard unqualified opinion, the 2019-2020 audit report of SCCIG audited by Baker Tilly China (special ordinary partnership) with standard unqualified opinion and the unaudited financial statements for the first three quarters of 2021 as disclosed by the company; 2. The adjusted financial data and indicators are adjusted by S&P Global (China) Ratings; 3. "--" represents data unavailable.

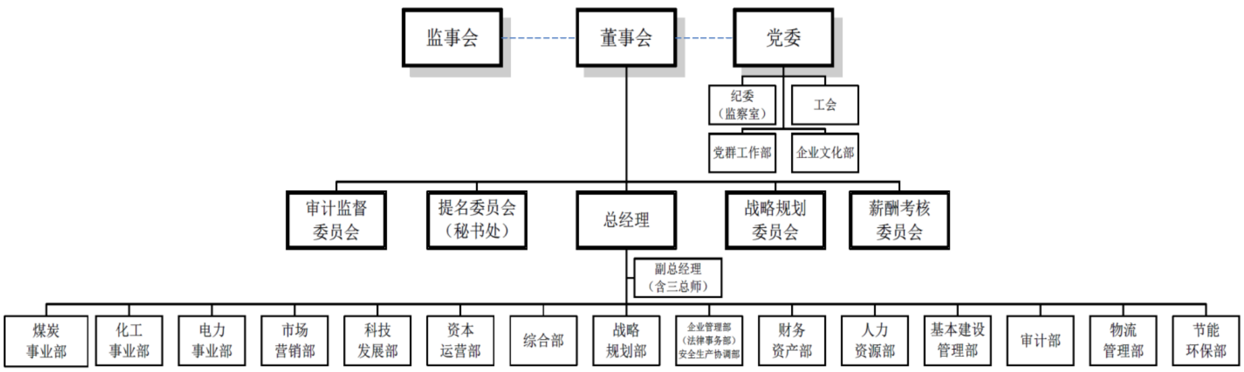
Source: Wind, S&P Global (China) Ratings.

Appendix 2: Ownership Structure of the Rated Entity (as of the end of September 2021)



Source: Wind, S&P Global (China) Ratings.

Appendix 3: Organizational Structure of the Rated Entity (as of the end of September 2021)



Source: Wind, S&P Global (China) Ratings.

Appendix 4: Key Terms

Key terms
EBITDA (reported) = Revenue - COGS - SG&A - R&D + D&A(reported) - Taxes and surcharges - Other operating expenses(income)
EBITDA = EBITDA (reported) + OLA rent - Capitalized development cost + Capitalized interest in COGS + Dividend received from equity investments + Other adjustments
D&A = D&A (reported)+ OLA depreciation + Other adjustments
EBIT = EBITDA (reported) + OLA rent - Capitalized development cost + Capitalized interest in COGS - D&A + Non-operating income (expense) + Other adjustments
Interest expense = Interest expense (reported) + Capitalized interest + OLA interest expense + Hybrid dividend accrual + Other adjustments
Cash interest paid = Cash Interest expense + Hybrid dividend cash payment + Other adjustments
FFO = EBITDA - Interest expense + Interest and dividend income - Current tax + Other adjustments
CFO = CFO (reported) + OLA depreciation - Capitalized development cost - Hybrid dividend cash payment - Cash interest expense + Dividends received + Other adjustments
Capital expenditure = Capital expenditure (reported)- Capitalized development cost + Other adjustments
FOCF = CFO - Capital expenditure
Dividends = Cash dividends + Dividends to minority interest - Hybrid dividend cash payments
DCF = FOCF - Dividends
Short-term debt = Shot-term loan + Financial liabilities held for trading + (Account payable - margin for payables) + Current portion of non-current liabilities (interest-bearing) + Interest payable + Other interest-bearing short-term debt
Long-term debt = Long-term loan + Bond + Financial lease payable + Lease obligation + Provisions - Guarantees & litigations + Other interest-bearing long-term debt
Debt = Short-term debt + Long-term debt + OLA debt - Surplus cash + Asset retirement obligation debt adjustment + Hybrid securities + External guarantees & litigations + Other adjustments
Capital = Total equity - Hybrid securities + Debt + Deferred taxes + Other adjustments
EBITDA interest coverage = EBITDA/Interest expense
FFO interest coverage = (FFO + Interest expense)/ Cash interest paid
ROC = EBIT/Two-year average capital
EBITDA Margin = EBITDA/Revenue

Appendix 5: Ratings Definitions

Ratings	Definition
$AAA_{spc(u)}$	The obligor's repayment ability is extremely strong, generally not impacted by any adverse economic environment, and the default risk is extremely low.
$AA_{spc(u)}$	The repayment ability is very strong, not considerably impacted by any adverse economic environment, and the default risk is very low.
$A_{spc(u)}$	The repayment ability is comparatively strong, comparatively vulnerable to the impact of adverse economic environment, and the default risk is comparatively low.
$BBB_{spc(u)}$	The repayment ability is average, comparatively impacted by adverse economic environment, and the default risk is average.
$BB_{spc(u)}$	The repayment ability is comparatively weak, materially impacted by adverse economic environment, and the default risk is comparatively high.
$B_{spc(u)}$	The repayment ability relies comparatively on fair economic environment and the default risk is very high.
$CCC_{spc(u)}$	The repayment ability relies extremely on fair economic environment and the default risk is extremely high.
$CC_{spc(u)}$	Lower protection in situation of bankruptcy or reorganization and the repayment of debt may not be generally guaranteed.
$C_{spc(u)}$	Unable to repay the debt.

Note: except for $AAA_{spc(u)}$ rating, CCC $_{spc(u)}$ and all ratings below may be added a "+" or "-" sign for minor adjustment to indicate a slightly higher or lower rating.

Appendix 6: Surveillance Plan

When the rating is valid, S&P Global (China) Ratings will monitor the available information concerning the entity, and if necessary, we may revise the rating.