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S&P Global
China Ratings

A Closer Look at China's LGFVs: Shandong

June 4, 2020

Key Takeaways

- Following a desktop analysis of 131 local government financing vehicles (LGFVs) in Shandong Province, we believe that the median indicative issuer credit quality of vehicles in the region is higher than the national median level.
- We believe that Shandong's 16 prefecture-level cities generally have strong indicative support capacity for their LGFVs, with Qingdao, Jinan and Yantai standing out in particular.

PRIMARY ANALYST

Lei Wang
Beijing
+86-10 6516 6038
lei.wang@spgchinaratings.cn

SECONDARY ANALYSTS

Di Jiao
Beijing
+86-10 6516 6039
di.jiao@spgchinaratings.cn

Xiao Zhang
Beijing
+86-10 6516 6036
xiao.zhang@spgchinaratings.cn

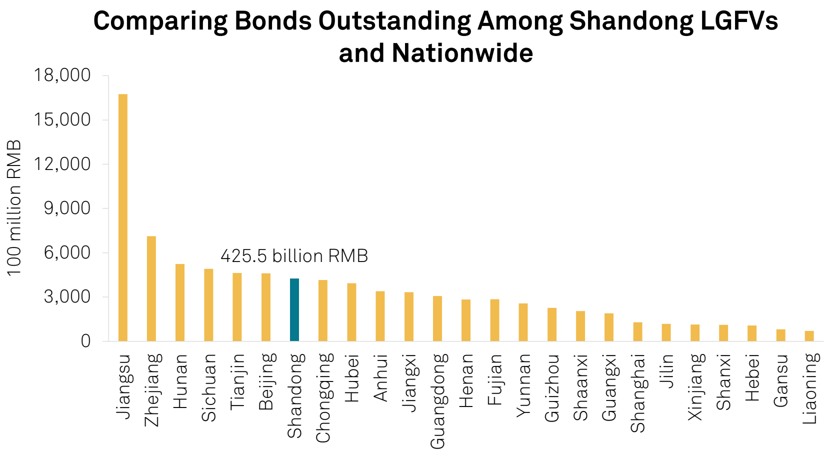
Yunxin Jia
Beijing
+86-10 6516 6041
yunxin.jia@spgchinaratings.cn

Ye Liu
Beijing
+86-10 6516 6035
ye.liu@spgchinaratings.cn

To get a full picture of the overall credit quality of LGFVs in Shandong Province, we carried out a desktop analysis of 131 LGFVs in the region, using public information. Our sample includes LGFVs at the city-level and below and subway companies, but excludes provincial-level LGFVs (like transportation construction companies, investment holding companies and utility companies). The entities in the sample represent close to 85% of LGFVs with bonds outstanding in Shandong, covering 16 prefecture-level cities. We believe they offer a comprehensive reflection of the overall indicative credit quality of LGFVs in Shandong.

We believe local government support is generally the most important factor when considering the indicative credit quality of LGFVs. In this report, we have analyzed the importance of LGFVs to Shandong's municipal governments, and the municipal governments' indicative ability to provide vehicles with support.

Chart 1



Note: LGFV debt defined by Wind, data as of December 31, 2019.
Source: Wind, S&P Global (China) Ratings.

About This Article

S&P Ratings (China) Co., Ltd. (S&P China) has conducted a desktop analysis of a selection of entities based in the relevant region. We have chosen these entities based on their asset sizes, representativeness of most regions and availability of public information. The analysis contained herein has been performed using S&P China Methodologies. S&P China Methodologies and analytical approaches are intended specifically for use in China only, and are distinct from those used by S&P Global Ratings. An S&P China opinion must not be equated with or represented as an opinion by S&P Global Ratings, or relied upon as an S&P Global Ratings opinion.

This desktop analysis has been conducted using publicly available information only, and is based on S&P China's methodologies for corporates. The analysis involves a desktop application of our methodologies to public information to arrive at a potential view of credit quality across sectors. It is important to note that the opinions expressed in this report are based on public information and are not based on any interactive rating exercise with any particular entity. The opinions expressed herein are not and should not be represented as a credit rating, and should not be taken as an indication of a final credit rating on any particular entity, but are initial insights of potential credit quality based on the analysis conducted. This desktop analysis does not involve any surveillance. The opinions expressed herein are not and should not be viewed as recommendations to purchase, hold, or sell any securities or to make any investment decisions, and do not address the suitability of any security.

We have conducted this desktop analysis on individual corporates and present the results contained herein at an aggregate group level. The different sections of this research show the statistics and performance of different groups of entities and the market more broadly against the metrics we generally consider most relevant under our methodologies.

Given the desktop nature of this analysis, and that we have not conducted an interactive review with any particular entity, we may have made certain assumptions in lieu of confirmed information and where relevant we may also have attempted to consider any possibility of parent, group, government or other forms of potential support, to inform our view of potential credit quality. S&P China is not responsible for any losses caused by reliance on the content of this desktop analysis.

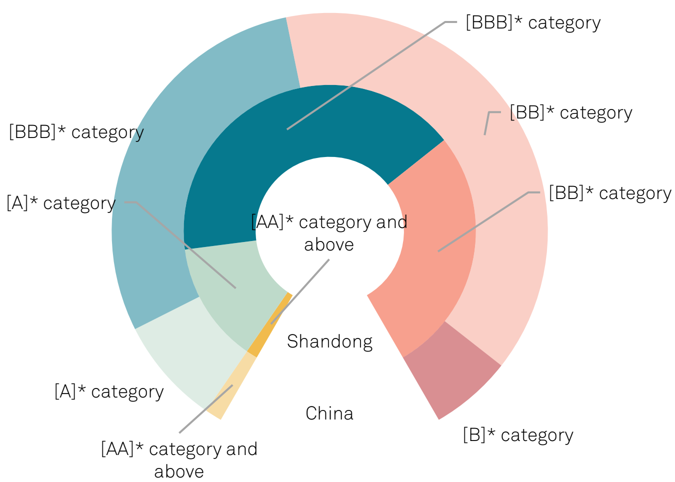
On the National Level: Shandong LGFVs Stronger Overall

As one of China's most developed provinces, Shandong is at the forefront nationwide in terms of its economic and financial strength. In 2019, Shandong's GDP was 7.1 trillion RMB, ranking third nationally, while its per capita GDP of 70,653 RMB is at the national average level. In terms of its industrial structure, Shandong's primary, secondary and tertiary industries accounted for 7.2%, 39.8% and 53.0% respectively. In 2019, Shandong's general public budget revenue was 652.7 billion RMB, with a general public budget balance ratio of -65%, a good level when compared to other regions. Shandong's key industries include chemicals, energy, metals, mining, agriculture and food processing.

When compared to a national sample of 1700 LGFVs, the median indicative issuer credit quality of the 131 vehicles in our sample is higher. We believe this can largely be attributed to cities in Shandong generally having strong indicative support capacity.

Chart 2

Indicative Credit Quality: Comparing LGFVs in Shandong and Nationwide



Note*: The indicative credit quality distributions expressed in this report are only S&P China's indicative views of credit quality derived from a desktop analysis based on public information without interactive review with any particular entity or the full credit rating process such as a rating committee. The opinions expressed herein are not and should not be represented as a credit rating and should not be taken as an indication of a final credit rating on any particular entity. Curve represents the proportion of companies in the sample.
Source: S&P Global (China) Ratings.

Within the Province: LGFVs Vary in Terms of Indicative Issuer Credit Quality

Our analysis found that the business and financial risk profiles of LGFVs are largely similar, and there are fewer differences between LGFVs in terms of indicative stand-alone credit quality. Differences in credit quality among LGFVs can largely be attributed to differing levels of government support. We believe that differences in the degree of support largely stem from variations in the indicative support capabilities of local governments and LGFVs' different levels of indicative importance to their relevant local authorities.

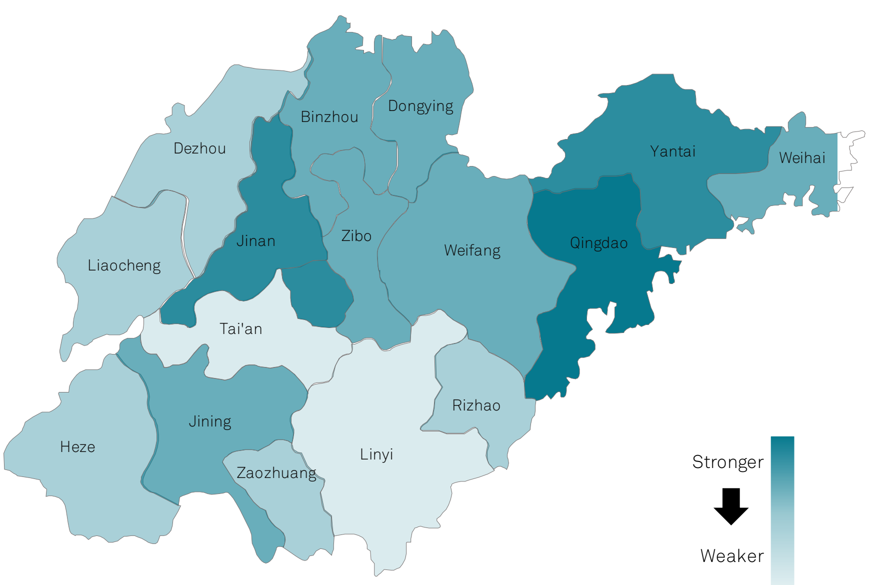
Analysis of Local Government Indicative Support Capacity

In terms of local government support capability, we looked at each of Shandong's 16 prefecture-level cities and considered factors such as economic performance, budget, debt, liquidity and financial management. Our analysis suggests that while Shandong's cities generally have strong indicative support capabilities, some differences can be found. Qingdao, Jinan and Yantai can provide a stronger level of support to LGFVs, while Tai'an and Linyi are at the opposite end of the spectrum in the province.

The chart below shows the indicative support capability of local governments for LGFVs across Shandong. The darker the color, the stronger the indicative support capability for LGFVs, and vice versa. As can be seen below, the province is stronger to the east and weaker towards the west in terms of its cities' indicative support capabilities for LGFVs.

Chart 3

Varied Indicative Ability to Support in the Province

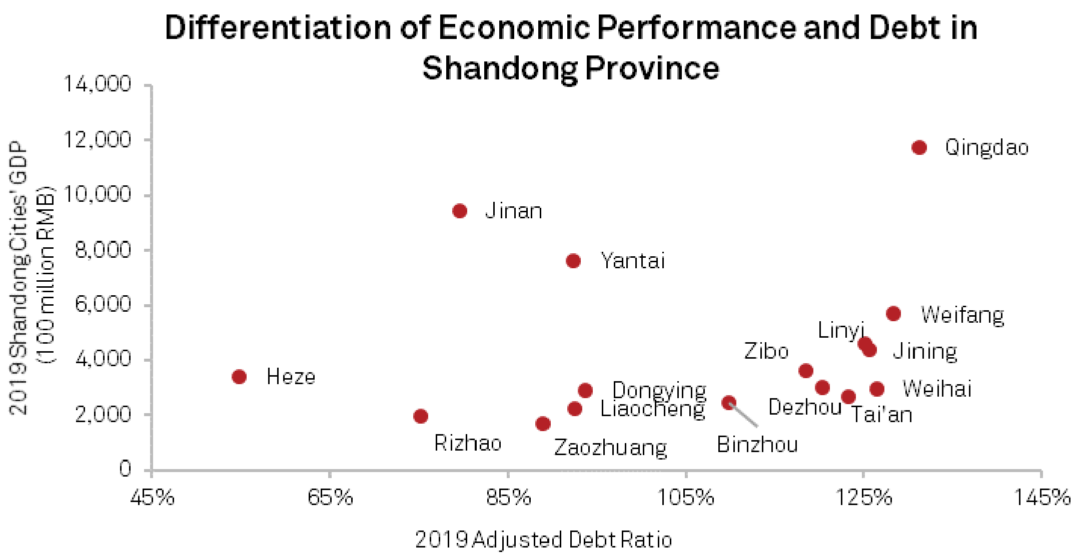


Note: Laiwu city is now under Jinan's jurisdiction.
Source: S&P Global (China) Ratings.

We believe that differences in economic and financial strength, as well as the debt situation of cities in Shandong may lead to local authorities having different indicative support capabilities.

Qingdao is Shandong's strongest city in terms of its economy, but it also has the province's highest debt ratio. This is mainly because of the city's large-scale investment in infrastructure construction and use of capital market financing, which has led to significant LGFV debt levels. The provincial capital Jinan and Yantai are second only to Qingdao in terms of economic strength. However, Jinan's debt ratio is at the lower end for the province, with low levels of both government debt and LGFV debt. At the same time, we found that while Rizhao and Zaozhuang have smaller economies than other cities in the province, they have relatively low debt ratios. This is mainly because both cities have low LGFV debt levels.

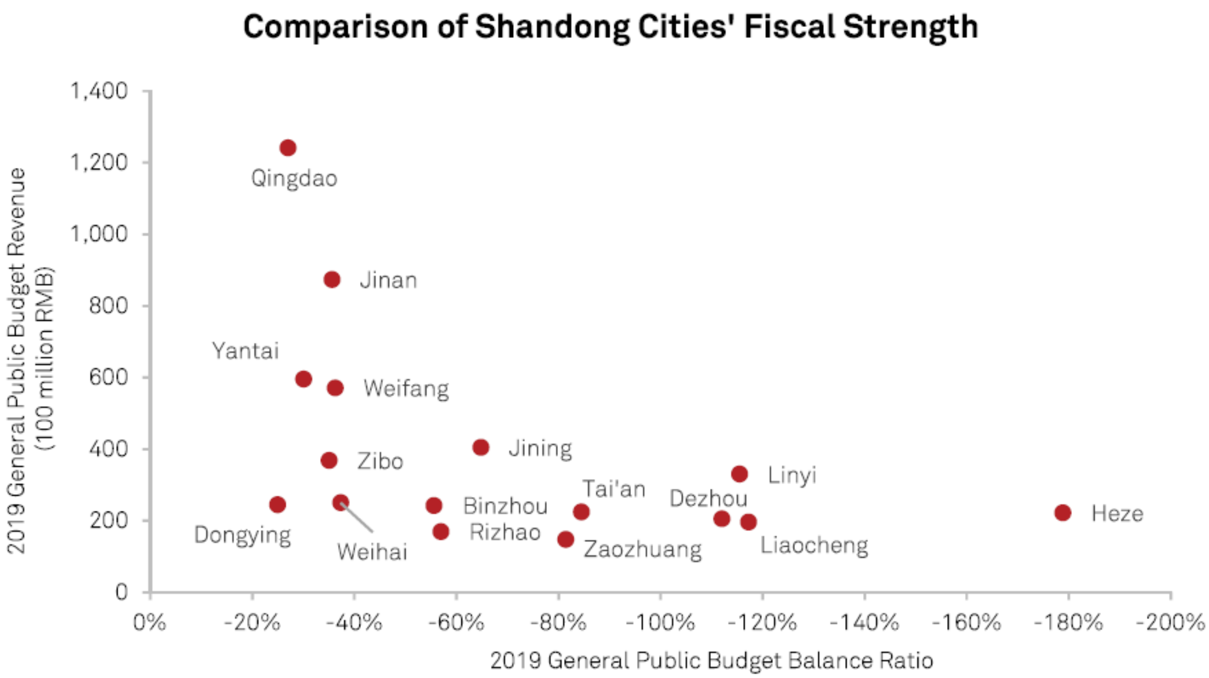
Chart 4



Note: Adjusted Debt Ratio=(2019 gov. debt + estimated 2019 adjusted LGFV debt)/2019 fiscal revenue.
Source: Wind, S&P Global (China) Ratings.

Qingdao and Jinan are the province's strongest cities in terms of fiscal strength, with large-scale fiscal revenue and good capacity to balance their public budgets. This fiscal strength can be attributed to both cities' good economic situations. Although Rizhao, Dongying, Binzhou and Weihai have smaller general public budget revenue, their populations are small. This means they have lower non-discretionary general budget expenditure, thereby better capacity to maintain their general public budget balance. However, Heze has relatively low fiscal revenue and a large population, pushing the city's general public budget balance ratio to the lower end for the province.

Chart 5



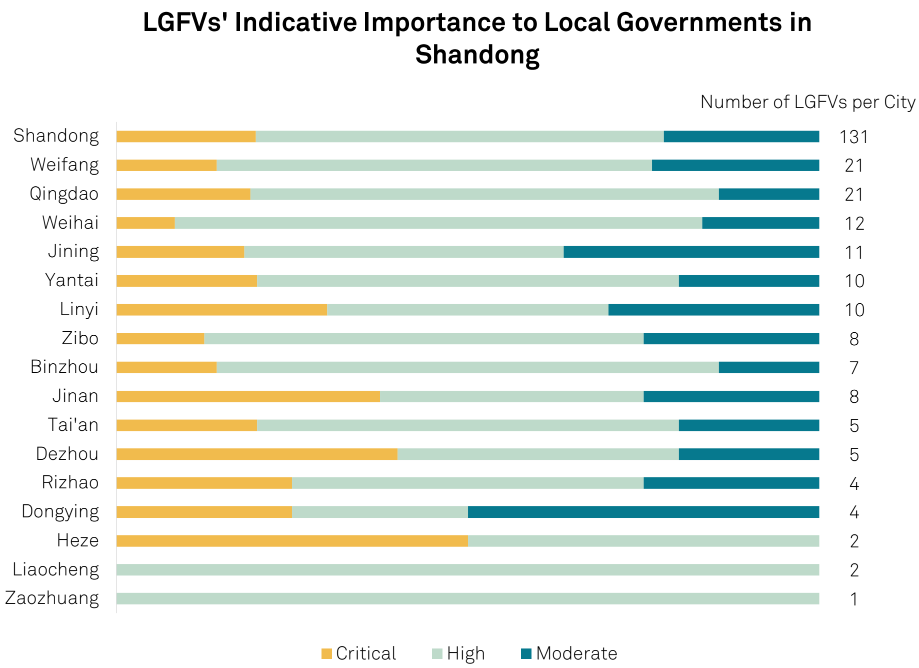
Source: Government websites, S&P Global (China) Ratings.

Analysis of LGFVs' Importance to Local Governments

In addition to each government's indicative capability to support, differences in the indicative issuer credit quality of LGFVs also depend on an LGFV's indicative importance to its relevant government. When analyzing support, we typically consider an LGFV's importance by looking at factors such as: its administrative level; its policy role; whether its business is not-for-profit or difficult to replace; revenue and asset scale; strategic importance, etc.

The chart below presents an overview of the distribution of LGFVs' indicative importance to their local governments in Shandong and its prefecture-level cities. Differences can be found between different cities in terms of the distribution of their LGFVs' levels and functions, leading to a broad range of indicative importance.

Chart 6



Source: S&P Global (China) Ratings.

Compared to other cities in the province, Zaozhuang, Liaocheng and Heze have a lower number of LGFVs. The majority of Zaozhuang and Liaocheng's LGFVs operate at a district or county level. While these vehicles may take on more functions in their respective districts or counties, we believe that their lower levels mean that they are only of high importance to their local governments rather than critical. Weifang and Qingdao, on the other hand, have a higher number of LGFVs, with each city having more than 20 vehicles under their jurisdiction. However, a high proportion of LGFVs in these cities are at a medium or low level, and some regions include multiple vehicles with overlapping functions. Provincial capital Jinan has a relatively small amount of LGFVs, with 8 vehicles under its jurisdiction. With a clear distribution of levels and well-defined functions, we believe Jinan's LGFVs are evenly distributed in terms of their indicative importance to their local government.

Distribution of Indicative Issuer Credit Quality Across Different Cities

There are some differences between cities in Shandong in terms of their indicative support capabilities for LGFVs. This, along with clear differences in LGFVs' indicative importance to local authorities, leads to a relatively scattered distribution of indicative issuer credit quality among LGFVs in Shandong's cities, as can be seen in the chart below.

Chart 7

Distribution of Indicative Issuer Credit Quality Across Shandong LGFVs

Note: Municipalities are in alphabetical order. The horizontal axis represents LGFVs' indicative issuer credit quality. The closer to the left, the stronger the indicative issuer credit quality.The color represents the number of LGFVs with the same indicative issuer credit quality. The darker the color, the higher the number of entities. The dark dotted line represents the median of indicative credit quality of Shandong Province.

Source: S&P Global (China) Ratings.

Qingdao, Linyi, Weihai, Jining, Weifang and Yantai have a relatively higher number of LGFVs. Because of differences in their levels and functions, there may be some differentiation between LGFVs in terms of their indicative importance to local governments, and a greater dispersal of indicative issuer credit quality. Qingdao, in our view, has the strongest indicative support capacity, and its LGFVs therefore tend to be stronger overall than the provincial median. Compared to elsewhere in the province, local authorities in Rizhao, Zaozhuang and Tai'an are relatively weaker in terms of indicative support capacity, and their LGFVs have lower median indicative issuer credit quality than the provincial median.

Related Research

- A Closer Look at China's LGFVs: Sichuan, May 21, 2020
- A Closer Look at China's LGFVs: Chongqing, May 21, 2020
- A Closer Look at China's LGFVs: Yunnan, May 21, 2020
- A Closer Look at China's LGFVs: Jiangxi, May 11, 2020
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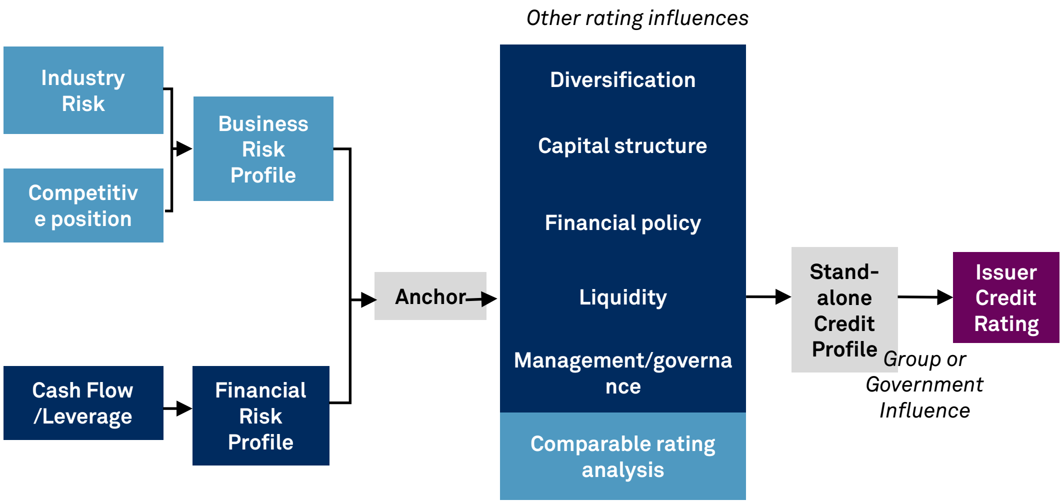
- A Closer Look at China's LGFVs: Zhejiang, April 2, 2020
- Looking Beyond the Short Term – Corporate Outlook: 2020, March 4, 2020
- A Group Portrait of China's LGFVs, November 4, 2019
- Looking For The Most Resilient Players, November 4, 2019

Appendix 1

S&P Global (China) Ratings' Corporate Methodology Framework



This report does not constitute a rating action.

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