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S&P Global China Ratings

2026 LGFV Credit Outlook: Mergers & Integrations to Intensify, Differentiation in Resources and Policy Coordination to Drive LGFV Credit

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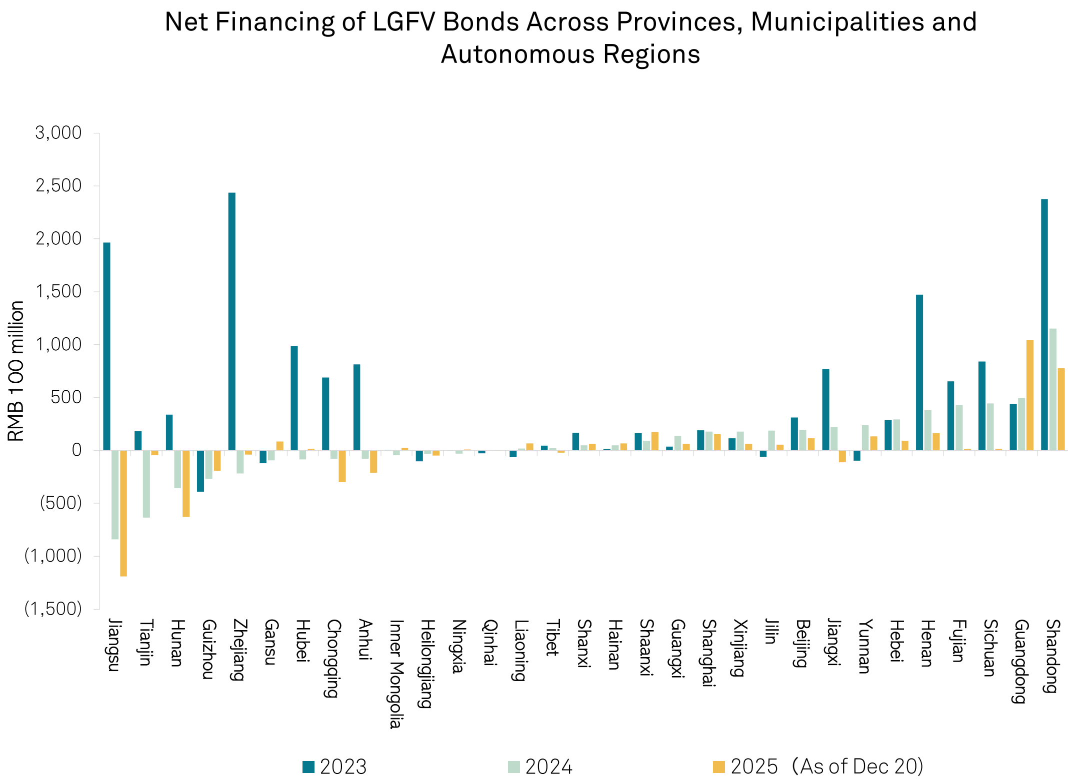
In recent years, with the continuous advancement of local government debt resolution, the exit and transformation of local government financing vehicles (LGFVs) have become a focal point for both policy makers and market participants. In 2025, the credit quality of the LGFV sector remained relatively stable, supported by favorable conditions such as debt swaps, resolution of implicit debt, and declining financing costs. We believe the refinancing environment, policy direction, transformation pathways, and credit evolution for LGFVs in 2026 will exhibit the following key trends.

Trend 1: Refinancing Environment Stay Tight, with Liquidity Pressures Driving Continued Non-Standard Asset Risk Exposure

We expect the refinancing environment for LGFVs to remain tight in 2026, with strict controls continuing on new LGFV financing. 2026 marks the crucial final year for resolving RMB 10 trillion of implicit debt, with central and local policy focus remaining on addressing the stock and strictly controlling the increment of local implicit debt. We anticipate that strict policies regarding new bond issuance financing, list-based management, and the rollover of non-standard financing for LGFVs will persist in 2026. New financing for LGFVs on the regulatory list will continue to face significant restrictions. For entities not on the list, while there may be no explicit regulatory red lines, they will still need to meet requirements such as the "335" rules and interest coverage ratios, and the success of obtaining new financing remains highly uncertain. Looking at net financing volume, since 2024, the net financing scale of LGFV bonds has declined significantly compared to previous years. Traditional major LGFV provinces are mostly in a state of net outflow, while regions with net financing inflows are primarily those with historically relatively lower debt burdens. Against the backdrop of stringent control over local government debt risks, we expect that the financing environment for LGFVs in 2026 will remain tight.

Chart 1



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

We expect the trend of risk exposure in LGFVs' non-standard financing to continue in 2026. The capacity of operating cash flow to cover interest payments remains weak. Therefore, platforms or regions with limited ability to increase indirect financing will face significant pressure in meeting interest payments. In such situations, constrained by insufficient support capacity, a platform's non-standard debts are likely to become the first buffer to be sacrificed to ensure bond repayments. Regions where fiscal revenue is relatively small compared to the scale of local debt/LGFVs will bear the brunt of this issue.

Table 1: Counties/Districts with LGFV Debt to General Public Budget Revenue > 15x

District/County	City	Province	General Public Budget Revenue (RMB 100 million)
Shanghang County	Longyan City	Fujian Province	38
Zhongshan District	Liupanshui City	Guizhou Province	12
Beihu District	Chenzhou City	Hunan Province	9
Hetang District	Zhuzhou City	Hunan Province	4
Lusong District	Zhuzhou City	Hunan Province	6
Shifeng District	Zhuzhou City	Hunan Province	7
Taoyuan County	Changde City	Hunan Province	15
Gaochun District	Nanjing City	Jiangsu Province	44
Jintan District	Changzhou City	Jiangsu Province	61
Lishui District	Nanjing City	Jiangsu Province	71
Liuhe District	Nanjing City	Jiangsu Province	51
Pukou District	Nanjing City	Jiangsu Province	67
Rugao City	Nantong City	Jiangsu Province	80
Yizheng City	Yangzhou City	Jiangsu Province	52
Hanting District	Weifang City	Shandong Province	22
Chenghua District	Chengdu City	Sichuan Province	63
Chuanshan District	Suining City	Sichuan Province	5
Gaoping District	Nanchong City	Sichuan Province	8

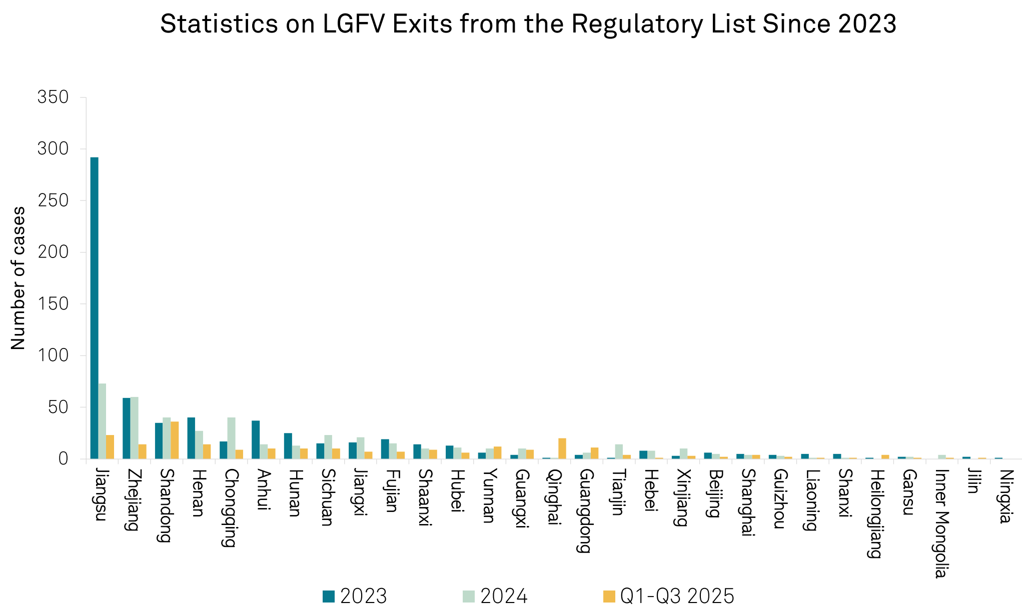
Jialing District	Nanchong City	Sichuan Province	9
Jianyang City	Chengdu City	Sichuan Province	38
Pengzhou City	Chengdu City	Sichuan Province	43
Pidu District	Chengdu City	Sichuan Province	64
Qingbaijiang District	Chengdu City	Sichuan Province	52
Wenjiang District	Chengdu City	Sichuan Province	59
Xindu District	Chengdu City	Sichuan Province	70
Nanxun District	Huzhou City	Zhejiang Province	44
Jizhou District	-	Tianjin Municipality	15
Anji County	Huzhou City	Zhejiang Province	63
Shengzhou City	Shaoxing City	Zhejiang Province	52
Fuyang District	Hangzhou City	Zhejiang Province	101
Xinchang County	Shaoxing City	Zhejiang Province	50
Wuxing District	Huzhou City	Zhejiang Province	68
Zhuji City	Shaoxing City	Zhejiang Province	100
Tonglu County	Hangzhou City	Zhejiang Province	46
Changxing County	Huzhou City	Zhejiang Province	89
Shangyu District	Shaoxing City	Zhejiang Province	98
Haining City	Jiaxing City	Zhejiang Province	102
Deqing County	Huzhou City	Zhejiang Province	85
Longgang City	Wenzhou City	Zhejiang Province	21
Lanxi City	Jinhua City	Zhejiang Province	39
Putuo District	Zhoushan City	Zhejiang Province	34
Ouhai District	Wenzhou City	Zhejiang Province	43
Keqiao District	Shaoxing City	Zhejiang Province	144
Wucheng District	Jinhua City	Zhejiang Province	15
Huangyan District	Taizhou City	Zhejiang Province	51
Dongtou District	Wenzhou City	Zhejiang Province	11
Banan District	-	Chongqing Municipality	39
Nanchuan District	-	Chongqing Municipality	29
Qijiang District	-	Chongqing Municipality	23
Shapingba District	-	Chongqing Municipality	37
Changshou District	-	Chongqing Municipality	52

Note: General Public Budget Revenue data is for 2024.
Source: Public information, S&P Global (China) Ratings compilation.

Trend 2: Transformation is Imperative, Mergers & Integrations to Continue, Credit Differentiation to Stem from Transformation Choices and Resource Access

We believe that being on the regulatory list is not the core indicator determining the function, regional status, and credit quality differentiation of LGFVs, because clearing implicit debt and no longer undertaking government financing functions—as stipulated by exit criteria—are eventual goals for all LGFVs. Since the State Council issued the "Notice on Strengthening the Management of Local Government Financing Platform Companies" (State Document [2010] No. 19) in 2010, LGFVs have gradually entered a phase of orderly supervision and development. The "list-based" monitoring and management of platform companies became an important part of debt resolution. Particularly after the introduction of “Document No. 150" in August 2024, policies further clarified the standards and timelines for LGFVs to exit the platform list, accelerating the exit process. According to "Document No. 150," exiting the platform list requires meeting the following conditions: 1) completion of implicit debt clearance; 2) explicit commitment to no longer undertake local government financing functions; and 3) obtaining consent from two-thirds or more of commercial financial creditors. Creditors who disagree must provide their own evidence. Furthermore, the deadline for exiting the platform list is no later than the end of June 2027, meaning the announcement of LGFV exits will continue to advance over the next two years.

Chart 2



Note: The statistical period covers from 2023 to September 30, 2025.
Source: www.qyyjt.cn, compiled by S&P Global (China) Ratings.

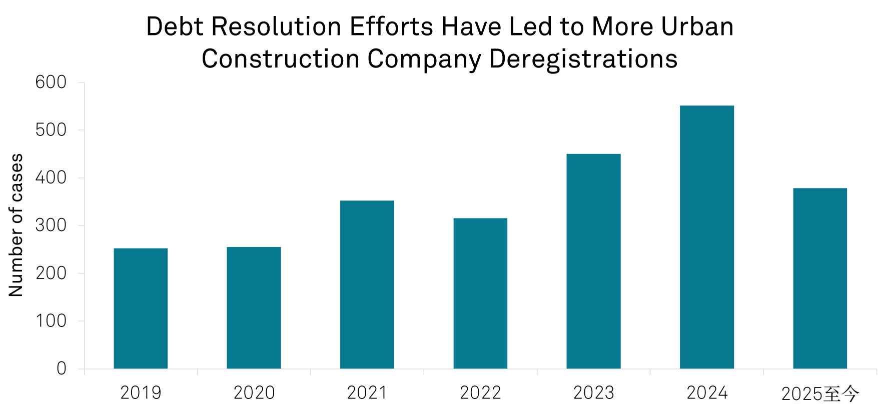
We believe that in the transformation of LGFVs, the choice of transformation direction and the ability to access resources will be the core factors driving future credit differentiation among platforms. Constrained by objective factors such as access to industrial resources, talent allocation, and team development within platform companies, we believe it is very difficult for platform companies to transform into fully market-competitive industrial enterprises. Excessive debt from purely market-oriented businesses unrelated to regional development would also significantly dilute external support, ultimately weakening corporate credit quality. We consider that there are currently two more realistic transformation paths: one is transforming into a regional operator, shifting from regional construction to asset operation; the other is transforming into an industrial investment platform primarily aimed at serving regional economic development and promoting industrial project implementation. The foundation for these two types of transformation lies in the ability to secure resource integration or policy support within the region. However, given the scarcity of such resources within regions, the ability to obtain resources will directly determine the success of such transformations, constituting one of the main sources of future credit differentiation among LGFV platforms.

Chart 3: LGFV Transformation Paths, Difficulty Levels, and Credit Impact

	Traditional Business: Undertake Government Financing Function	Agency Construction, Government Procurement Services & "Self-operated Projects"	Urban Operators & Industrial Investors	Full Marketization: Participating in Market Competition
Business Details	• Directly undertake financing function for local governments • Not in line with current policy requirements	• Distinguish by whether the underlying project generates cash flow. • No cash flow: Replace government-financed infrastructure construction with an agency construction model • Has cash flow: Convert into enterprise "self-operated projects" — independent project approval, financing, construction, and operation.	• Operate various urban assets that have direct cash flow or fee rights • Equity investment oriented toward serving regional economic development and promoting industrial project implementation.	• Fully participate in market-oriented competition, and even go beyond their local regions to operate industrial businesses
Transformation Difficulty levels	• No further new projects • Existing debts will be gradually resolved	• Currently mainstream business model of LGFVs, comply with policy requirements	• Medium difficulty: mainly constrained by resource acquisition and policy access capabilities	• High difficulty: constrained by objective factors such as industrial resources and talent acquisition
Impact on Credit	• N/A	• Not affect current credit quality as this is the current mainstream	• LGFVs that can integrate regional resources will have their credit quality strengthened, while platforms unable to secure sufficient resources may become marginalized.	• Credit quality will experience significant divergence. Fully market-oriented operations are very difficult to succeed in. An increase in businesses unrelated to serve the region may weaken external support

We expect that the number of LGFVs ultimately retained within the same region will significantly decrease in the future, with mergers and acquisitions (M&A) remaining a persistent theme. Considering that locally available operating assets capable of generating cash flow are relatively scarce, and many regions host numerous platforms, operating assets are insufficient to be allocated to all entities. Therefore, we believe M&A among LGFVs will continue to be a solution to resource scarcity and large number of LGFVs. During the M&A process, in regions with high debt ratios, some non-standard debts may be abandoned as a buffer to ensure bond repayments. Conversely, the consolidated entities that receive significant infusions of operating assets may continue to exist post-debt resolution, becoming important vehicles for the management of regional state-owned assets.

Chart 4



Note: 1. 2025 data as of December 20. 2. The statistical scope covers deregistered companies with "Urban Construction" in their names.
Source: www.qyyjt.cn, compiled by S&P Global (China) Ratings.

Trend 3: New Policies Expected to Succeed Previous Ones, Focusing on Controlling and Resolving LGFVs' Operating Debt

We expect that new policies targeting the existing debt of LGFVs may be gradually introduced in 2026, with a focus on guiding LGFVs to resolve their operating debt. According to the overall arrangement and pace of debt resolution, 2026 is a critical year for LGFV debt resolution. If the original plan of swapping RMB 2 trillion annually is executed as scheduled, implicit debt will decline to approximately RMB 4 trillion by the end of 2026. We believe that, whether from the perspective of consolidating debt resolution achievements or stabilizing local and regional financial environments, new policies will follow. The Central Economic Work Conference held in December this year proposed actively and orderly resolving local government debt risks, urging local governments to take initiative in debt resolution, prohibiting illicit additions to implicit debt, optimizing methods for debt restructuring and swaps, and employing multiple measures to resolve the operating debt risks of local government financing platforms. This statement sends a positive signal and marks the first time the highest policy level has explicitly mentioned resolving operating debt risks. Therefore, we believe that new policies may focus on addressing the risks associated with LGFVs' operating debt.

We believe that the pressure to resolve operating debt may be addressed through categorized approaches. Based on currently available policy tools, these may be divided into three types: special bond swaps, government repayments, and debt restructuring that extends the tenure and lowers the cost of existing debt. Regarding special bonds, the focus may be on repurchasing assets that can generate future cash inflows, such as further implementing land reserve special bonds or policies for repurchasing unsold commercial housing. Using these tools to repurchase LGFV assets could reduce operating debt. From the perspective of agreed government repayments, although many LGFVs have exited the regulatory list, they still hold many quasi-public welfare assets or assets that the local government is contractually obligated to repurchase gradually. Local governments may reduce LGFVs' operating debt through gradual repayments. We expect the goal of these multiple approaches is to enable LGFVs' operating cash flow to cover daily interest expenses, with the remaining principal being gradually turned over and revitalized over time.

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