Rating Action: **Moody's downgrades ratings of 17 Chinese LGFVs; changes outlooks to negative**

25 Jan 2024

Hong Kong, January 25, 2024 -- Moody's Investors Service has downgraded the ratings of 17 Chinese local government financing vehicles (LGFVs) by one notch from their previous levels, following the one-notch decline in the governmental capacity to support (GCS) score of the respective regional and local governments (RLGs) that own the LGFVs. The 17 LGFVs are owned by 12 provincial-, city- or district-level RLGs.

Moody's has changed the outlook on these LGFVs' ratings to negative, reflecting a potential weakening in the GCS scores of their respective RLG owners, given the negative outlook on China's sovereign rating. Previously, the ratings were on review for downgrade.

This concludes the rating review for the 17 LGFVs that was initiated on 6 December 2023.

Please click on this link https://www.moodys.com/viewresearchdoc.aspx?docid=PBC_ARFTL484363 for the List of Affected Credit Ratings. This list is an integral part of this Press Release and identifies each affected issuer.

RATINGS RATIONALE

Moody's has lowered the GCS scores of the 12 RLGs that own the 17 LGFVs by one notch. These RLGs include Shandong province (lowered to a2 from a1); Henan and Guangxi provinces (lowered to a3 from a2); Changsha and Zhengzhou city (lowered to baa1 from a3); Yinchuan, Lhasa and Linyi city (lowered to baa2 from baa1); Zhuzhou city and Yantai Zhifu district (lowered to baa3 from baa2); and Changde and Weifang city (lowered to ba1 from baa3). Medium-term credit challenges remain across the 12 RLGs, despite some liquidity relief from the Chinese government's support measures for LGFV debts.

The lowering of the GCS scores of the 12 RLGs is partly driven by Moody's view that central government support toward addressing direct and indirect debt at the regional level will be more selective, as indicated by the government's policy position, including its ongoing policy statements and actions. Although recent measures have allowed some provincial governments to issue bonds to address LGFVs' near-term maturities, the policies have stopped short of addressing long-term debt sustainability challenges, particularly following the increase in debt levels and the material decline in land sales revenue. Moody's assesses that additional central government measures to support RLGs in addressing their direct and indirect debt will be limited in scale and duration, given the government's emphasis that the responsibility of local debt lies at the RLG level.

The lowering of Shandong province's GCS score also reflects its weakened credit fundamentals, including its reduced land sales, high direct debt burden and increased liquidity pressure associated with state-owned enterprise (SOE) liabilities, including those of LGFVs and particularly at some lower-tier RLGs. The change in Shandong's GCS score has directly affected the GCS scores of Linyi city, Yantai Zhifu district and Weifang city, given the close links between the province and the RLGs below the provincial government.

The lowering of Henan province's GCS score also reflects its weakened credit fundamentals, including its expanded direct debt burden and elevated SOE liabilities. The change in Henan's GCS score has directly affected the GCS score of Zhengzhou city, given the close links between the province and the provincial capital.

The lowering of Guangxi province's GCS score also reflects its weakened credit fundamentals, including its expanded direct debt burden and elevated SOE liabilities.

Hunan province has experienced weakened credit fundamentals, including continued population outflow, reduced land sales, relatively high direct debt burden and elevated SOE liabilities. These factors have diminished Hunan's capacity to support lower-tier RLGs, and directly affected the GCS scores of Changsha, Zhuzhou and Changde city, given the close links between the province and the RLGs below the provincial government.

Tibet Autonomous Region has experienced weakened credit fundamentals, including extremely low fiscal self-sufficiency, scarce revenue sources and limited financial buffers, as well as relatively weak economic fundamentals and prospects. These factors have diminished Tibet's capacity to support lower-tier RLGs, and directly affected the GCS score of Lhasa, given the close links between the province and its provincial capital.

Ningxia Hui Autonomous Region has experienced weakened credit fundamentals, including weak economic prospects and pressure on the funding and liquidity conditions of Yinchuan's LGFVs. Despite recent government measures to enhance the LGFVs' access to funding, uncertainties remain around the sustainability of the improved funding conditions. These factors have diminished Ningxia's capacity to support lower-tier RLGs, and directly affected the GCS score of Yinchuan, given the close links between the province and its provincial capital.

The negative outlooks on the 17 LGFVs' ratings reflect Moody's expectation of a potential weakening of their respective RLG owners' capacity to support, given the negative outlook on China's sovereign rating. Under the agency's rating approach for LGFVs, an LGFV's rating is closely linked to its owner government's GCS score, which i turn is directly linked to China's sovereign rating.

The negative outlooks on Linyi City Development Group Co., Ltd (Ba1 negative), Shuifa Group Co., Ltd. (Baa2 negative) and Weifang Urban Construction and Dev Invt Grp (Ba2 negative) also reflect the issues affecting their respective owner governments' propensity to support, which were indicated in the negative outlooks on the companies prior to Moody's placing their ratings on review for downgrade.

FACTORS THAT COULD LEAD TO AN UPGRADE OR DOWNGRADE OF THE RATINGS

Given the negative outlooks, any upward rating pressure on these companies is unlikely.

Moody's could return the rating outlooks to stable if (1) the outlook on China's rating returns to stable; (2) changes occur in the RLGs' characteristics that lead to an increase in their governmental capacity to support; or (3) changes occur in the LGFVs' characteristics that could lead to an increase in their owner RLGs' propensity to support and offset the impact of weaker governmental capacity to support.

Moody's could downgrade the LGFVs' ratings if (1) China's sovereign rating is downgraded; (2) their owner RLGs' capacity to support weakens, which could arise from a material worsening of the RLGs' economic or financial profile or the governments' ability to coordinate timely support; (3) changes occur in the Chinese government's policies that prohibit RLGs from providing financial support to LGFVs; or (4) changes occur in the LGFVs' characteristics that could weaken their owner RLGs' propensity to support, such as diminished roles in key public projects.

PRINCIPAL METHODOLOGY

The principal methodology used in these ratings was Local Government Financing Vehicles in China Methodology published in April 2022 and available at https://ratings.moodys.com/rmc-documents/386644. Alternatively, please see the Rating Methodologies page on https://ratings.moodys.com for a copy of this methodology.

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The first name below is the lead rating analyst for this Credit Rating and the last name below is the person primarily responsible for approving this Credit Rating.

Stephen Tang
Asst Vice President - Analyst

Corporate Finance Group
Moody's Investors Service Hong Kong Ltd.
24/F One Pacific Place
88 Queensway
Hong Kong,
China (Hong Kong S.A.R.)
JOURNALISTS: 852 3758 1350
Client Service: 852 3551 3077

Ivan Chung
Associate Managing Director
Corporate Finance Group
JOURNALISTS: 852 3758 1350
Client Service: 852 3551 3077

Releasing Office:
Moody's Investors Service Hong Kong Ltd.
24/F One Pacific Place
88 Queensway
Hong Kong,
China (Hong Kong S.A.R.)
JOURNALISTS: 852 3758 1350
Client Service: 852 3551 3077

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