CCXI & CCXAP – Research & Commentary

The Net Financing of Urban Investment Bonds is Still under Pressure, and the Credit Differentiation May Further Intensify

Hong Kong, 2 September 2021 -- A report titled "The Net Financing of Urban Investment Bonds Decreased Year-on-Year, Credit Differentiation May Intensify Further - Market Operation of Urban Investment Bonds in the First Half of 2021" has been recently published by the Research Institute of China Chengxin International Credit Rating Co. Ltd. ("CCXI Research Institute"). According to the report, since the beginning of the year, a new round of strict supervision has resumed, and the pressure on the urban investment platform to obtain financing through bonds, credit, non-standard and other channels has increased. The net financing scale of urban investment bonds in the second half of the year may be roughly the same as that in the first half of the year, but it does not rule out the possibility of continuous tightening of policies and further decline of net financing. In the context of the continuous strict supervision policy on implicit debt, we need to continue to pay attention to the aggravation of regional and main financing differentiation, as well as the spread of non-standard default and guarantee risk under the background of limited urban investment and financing and debt repayment pressure.

The report systematically combs the operation of the urban investment bond market in the first half of the year. The report points out that affected by the tightening of the financing environment, the net financing scale of urban investment bonds has decreased significantly since this year, and the proportion of raised funds used to borrow new and repay old has further increased; The secondary market benefited from the shortage of high-quality assets of credit bonds and other factors, and the trading interest margin showed a downward trend as a whole. From the primary market, the issuance scale of urban investment bonds reached 2.73 trillion yuan, a year-on-year increase of 17.35% over the first half of 2020 and a month on month increase of 26.32% over the second half of 2020, accounting for an increase in credit bonds, but the net financing scale decreased by 26.89% over the same period last year to 963.94 billion yuan. Among them, the issuing scale of SCP financing accounts for the highest proportion, the issuance of urban investment bonds involving borrowing new to repay the old accounted for nearly 90%, and the proportion further increased. From the perspective of the secondary market, the transaction of urban investment bonds has obviously warmed up. The transaction scale of cash bonds has reached 5342.91 billion yuan, a year-on-year increase of 14.14%, accounting for 43.39% of the transaction scale of credit bonds, which continues to rise. The yield to maturity of urban investment bonds in each term showed a downward trend, with the short-end downward most obvious. In addition, there were many changes in bond transaction prices in the first half of the year in areas with weak economic and financial resources and low administrative level.

From the credit status of urban investment enterprises, a total of 27 Urban Investment platforms underwent level (outlook) adjustment in the first half of the year, mainly in the downward direction, but the number of non-standard defaults decreased in the same period. Among the 13 platforms with entity level adjustment, the main factors triggering the reduction of 6 entities are the deterioration of regional credit status and financing environment, the deterioration of main business collection, and higher contingent risks. The main factors triggering the increase of the seven entities include the enhancement of regional economic strength and the increase of government support. Among the 12 urban investment bonds involved in debt level adjustment, 11 were accompanied by subject level adjustment in the same period, and 1 was increased due to the increase of guarantee subject level. Among the 16 entities involved in the negative adjustment of rating outlook, 7 were the main entities, 8 were the debt, and 1 was included in the rating observation list. In terms of credit events, there were 16 non-standard defaults in the first half of the year, involving 31 urban investment platforms, and the number of non-standard defaults decreased by 48.39% year-on-year. The above urban investment platforms are mostly located in Guizhou in terms of geographical distribution, mostly at the district and county level in terms of administrative level, and most of the default products are trust plans.

Looking forward to the second half of the year, the net financing scale of urban investment bonds may not increase significantly compared with the first half of the year. Combined with the maturity and resale scale, the issuance scale of urban investment bonds is expected to be 2.6 to 2.8 trillion yuan. If the growth rate of stock social financing scale decreases slightly to about 11% in 2021, the stock scale of social financing may reach about 316 trillion yuan by the end of 2021. Assuming that the proportion of corporate bonds and asset-backed securities of deposit financial institutions in the scale of social financing continues to the current level, combined with the proportion of stock urban investment bonds in credit bonds, it is estimated that the scale of urban investment bonds at the end of the year is about 12.48 trillion yuan, and the net financing scale of urban investment bonds in the second half of the year is about 1 trillion yuan, which is basically the same as that in the first half of the year, However, it does not rule out the possibility that the continuous tightening of urban investment and financing policies may lead to a further decline in net financing. In addition, combined with the maturity and resale of urban investment bonds, it is estimated that the issuance scale of urban investment bonds in the second half of the year may be 2.6-2.8 trillion yuan.

Finally, the report reminds attention to the potential risks of urban investment enterprises. Firstly, pay attention to the spread of non-standard default and guarantee risk under the background of limited urban investment and financing and debt repayment pressure. In the context of tightening multiple financing channels, the liquidity pressure faced by the relatively large due debt burden of the urban investment platform in the second half of the year increased marginally. Considering the relatively strong signal significance of the bond market, in recent years, the urban investment platform tends to give priority to ensuring bond repayment when facing the pressure of debt repayment. Under the adverse impact of limited financing and pressure on debt repayment, some urban investment platforms that are difficult to sustain debt may first break out of non-standard default, and the ensuing guarantee risk may expand the scope. Secondly, we should pay attention to the possibility of intensified regional financing differentiation caused by policy impact. Since the beginning of the year, the exchange and dealers association have successively carried out debt ratio grading management for bonds issued by financing platforms, and the purpose of newly issued bonds and raised funds of financing platforms in red orange region has been limited to a certain extent; Recently, the China Banking and Insurance Regulatory Commission has also required banks and insurance institutions to strengthen regional risk management of financing platforms and set regional risk limits. The bank financing channels of relevant regional platforms may also be tightened, and the financing difficulty will increase marginally. In this context, the differentiation of regional financing environment may be more obvious, and the trend of investors holding together to strong strength regions and strong qualification platforms may be more obvious. Thirdly, pay attention to the liquidity pressure faced by the weakly qualified urban investment platform. On the one hand, in the first half of the year, the bond issuance policy faced by the weakly qualified urban investment platform was tightened, and the exchanges and dealers' associations issued regulations to implement classified management on the new bonds issued by the urban investment platform. On the other hand, in consideration of factors such as regional financing differentiation, some credit bond investors began to take the initiative to reduce their risk exposure to weakly qualified urban investment platforms. Overall, the marginal liquidity pressure faced by weak qualified urban investment platforms is rising, and it is necessary to continue to pay attention to the debt risk of relevant platforms in the second half of the year.

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