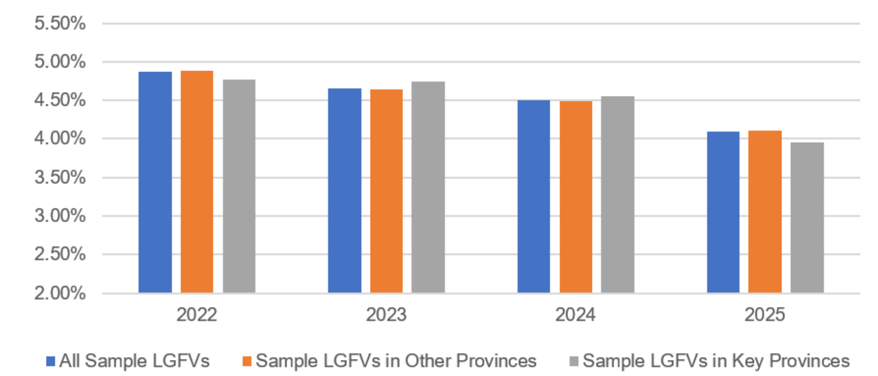
China's Debt Defusing Policies and "15th Five-Year Plan" for Urban Renewal Support the Transformation and Creditworthiness of LGFVs

China's local investment and development companies, also generally known as local government financing vehicles ("LGFVs"), are currently at a stage of reshaping their business and financing structures. With the advancement of debt defusing policies and improving financing environment, LGFVs' liquidity pressure eased, and financial transparency increased, creating space for their business transformation. At the same time, we consider that the Urban Renewal Plan during the 15th Five-Year Plan Period set a clear direction for the transformation of LGFVs, driving them to shift from traditional investment and financing platforms to investment and operation entities focusing on urban renewal and public services. The combined force of these policies not only supports the creditworthiness of LGFVs but also provides them with a sustainable development pathway for the future.

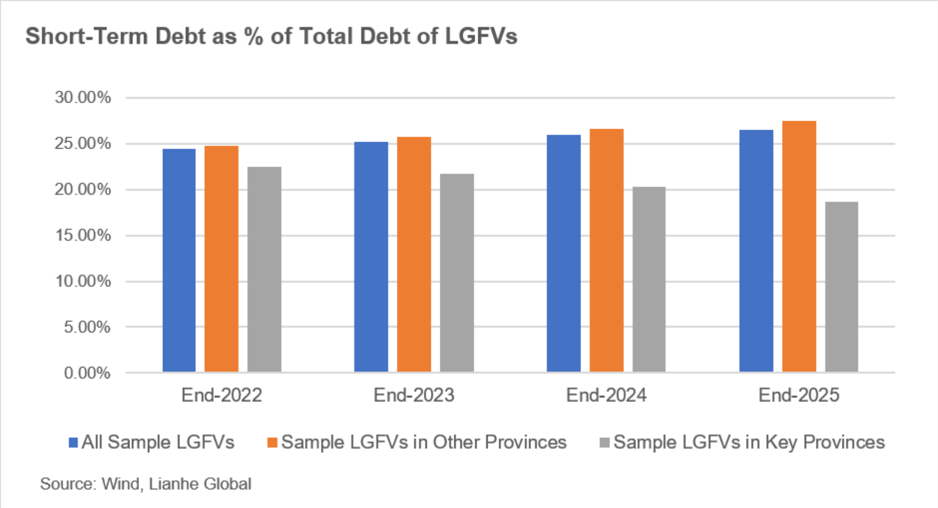
Debt Resolution Effectively Reduced Financing Cost and Improved Financing Structure

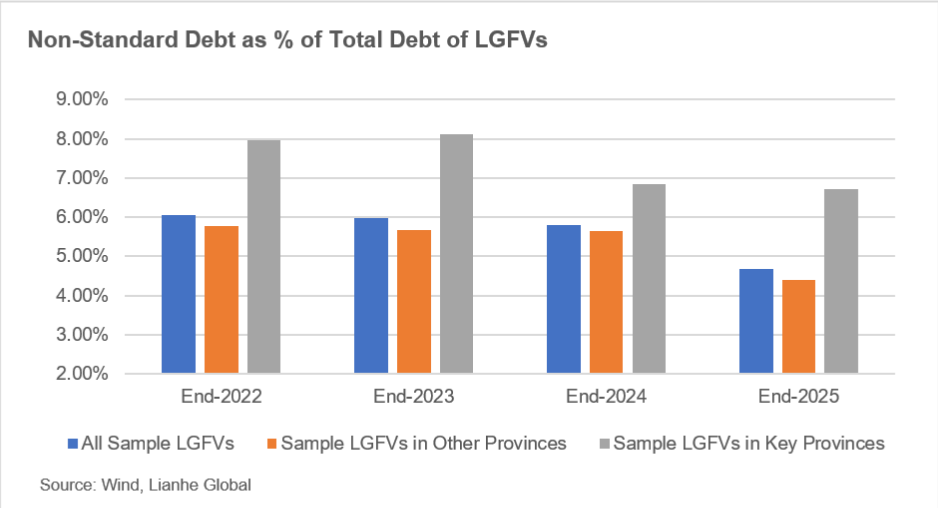
In recent years, China effectively reduced the financing costs of LGFVs and improved their financing structures through a series of debt defusing measures and a more proactive fiscal policy, while easing the debt burden of local governments. Among these measures, the issuance of local government special purpose bonds replaced short-term high-interest debt with long-term lower-cost debt. In 2025, local governments issued approximately RMB2 trillion bonds to replace existing hidden debts, reducing the average interest cost by more than 2.5 percentage points after the debt replacements. Simultaneously, bank loan extensions with interest rate reductions, together with the rigorous enforcement of the local government borrowing accountability system, effectively curbed the illegal addition of new hidden debts. In addition, the proactive clearance of government arrears to enterprises further lowered debt default risks. Overall, these measures collectively stabilized the liquidity of LGFVs, reduced debt rollover risks, and provided the necessary time and space for promoting their market-oriented transformation and sustainable development.

Composite Financing Cost of LGFVs



Source: Wind, Lianhe Global





Urban Renewal "15th Five-Year Plan" Drives Urban Upgrades

The State Council of China recently issued the Urban Renewal Plan during the 15th Five-Year Plan Period. The core objectives are to transform the models of urban development and construction, refine the systems and mechanisms for urban renewal, achieve significant improvements in the living environment by 2030, and build modern cities that are innovative, livable, beautiful, resilient, civilized, and smart by 2035. The key planning aspects include:

- **Creating high-quality living spaces:** Building safe, comfortable, green, and smart "quality homes"; renovating residential communities that are 20 years or older, developing 15-minute community life circles, and renovating old blocks and industrial zones while enhancing the quality of public services.

- **Improving comprehensive transportation and infrastructure:** Advancing road micro-circulation upgrades, renewing aging underground pipelines, and implementing safety projects for critical infrastructure lifelines.

- **Promoting green and low-carbon transformation:** Restoring urban ecosystems, retrofitting and upgrading high-energy-consuming public buildings, and developing sponge cities and green, slow-traffic transportation systems.

- **Upholding safety, resilience, and cultural prosperity:** Implementing the renovation of dilapidated housing and urban villages, advancing the construction of public infrastructure for both routine and emergency use, and ensuring the holistic preservation and revitalization of historic and cultural cities, districts, and industrial heritage.

Urban Renewal "15th Five-Year Plan" Improves the Investment and Financing System and Revitalizes Land Inventories

The Urban Renewal Plan during the 15th Five-Year Plan Period proposed to build a sustainable investment and financing system for urban construction and operation, establishing a reasonable cost-sharing mechanism among the government, the market, and residents. The policy clearly states that the central government supports urban renewals. Local government special-purpose bonds are permitted to back eligible urban renewal projects and may be used as project capital. Financial institutions are required to provide financial services for urban renewal projects in accordance with market-oriented and law-based principles, and shall not incur new implicit local government debt. At the same time, the Plan actively attracts private capital, promotes the issuance of infrastructure real estate investment trusts (“REITs”) and asset securitization products for eligible urban renewal projects, and supports enterprises in issuing corporate bonds, medium-term notes, etc.

In addition, the Plan proposed greater support for revitalizing land inventories. By regulating spatial composite utilization, encouraging multi-party cooperative redevelopment, and optimizing real estate registration services, it aims to more vigorously revitalize existing land and property resources, and provides transition-period policies, flexible land supply mechanisms, and streamlined registration procedures to facilitate urban renewal and industrial development.

Urban Renewal Facilitates the Transformation of LGFVs

We believe that urban renewals provide an opportunity to promote the transformation of LGFVs, with the impact mainly in three areas. First, LGFVs with asset operation capabilities can leverage urban renewal projects to expand and accelerate their shift into asset operation entities. By engaging in projects with stable cash flows such as government-subsidized housing, industrial parks, commercial properties, and infrastructure, LGFVs can revitalize existing assets and establish long-term sustainable income streams. Second, the policy encourages the use of capital market financing tools, such as REITs, asset securitizations, and corporate bonds, to broaden financing channels and enhance capital flows, helping LGFVs reduce reliance on land transfers and fiscal subsidies. Finally, with urban renewal projects encompassing old residential community renovations, infrastructure upgrades, and green, low-carbon construction, LGFVs can assume a more prominent role in public services and infrastructure operations, gradually transforming from traditional investment and financing platforms into specialized, market-oriented, and self-sustaining asset operation entities.

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