CreditSights

# China Property: Investor Meeting FAQs

27 Sep 2022, 12:58 PM

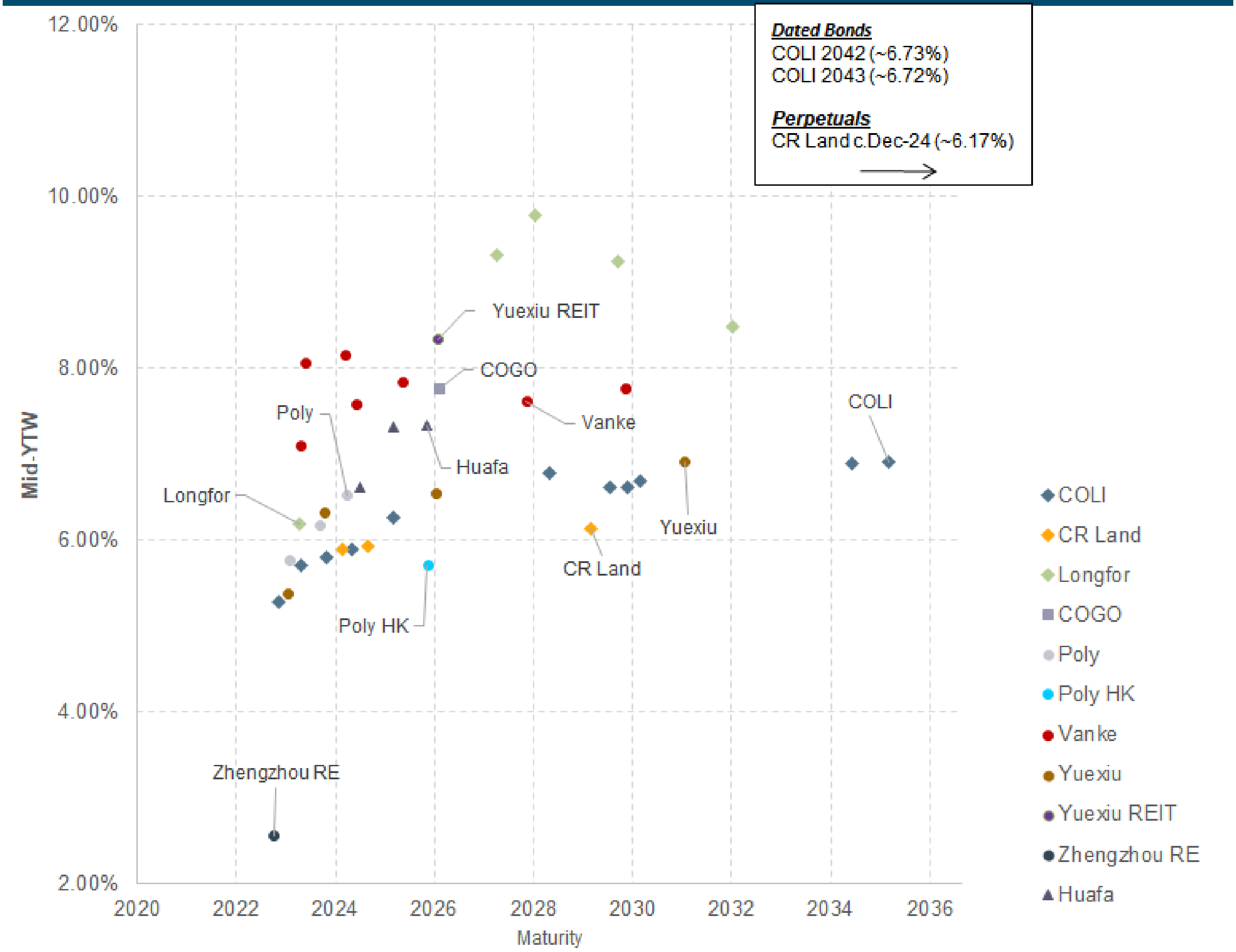
## Executive Summary

- **We recently concluded a series of meetings and calls on the China property sector with our clients.** We spoke to eleven accounts in Singapore, Hong Kong, Taiwan, Europe and the US, spanning a range of investor types, including asset managers, private banks, insurance firms and investment banks.
- **We compiled seven questions commonly raised by our clients in this report.** These are: (1) What are our expectations for the China property sector: will sales recover and will there be sector consolidation?; (2) Why hasn't there been a significant recovery in home sales in China?; (3) Is housing affordability deterring homebuyers in China?; (4) How effective are the recent liquidity support measures in helping the developers?; (5) What indicators should we look at to determine if a developer is able to survive?; (6) Are offshore investors still willing to be involved in this sector?; and (7) Which China property names do we recommend at this point?.
- **We expect more easing housing policies ahead in a bid by the Chinese authorities to boost home demand.** We also expect a further consolidation in the China property sector, though the pace of the consolidation is likely to be gradual.
- **The slew of easing measures have yet to transmit through the system and bear any significant fruit.** In our opinion, it is the unwillingness, rather than the inability, of homebuyers to purchase properties which has dampened home demand in China. In addition, we think the Chinese government still has an overarching mandate of "houses are for living in, not for speculation" in mind, and are likely reluctant to employ an "all-out easing" approach.
- **Most cash-strapped developers have resorted to disposing of assets and projects to raise funds or have conducted debt exchange offers to buy themselves some time.** On the other hand, selected "higher quality" developers have been able to tap onto the onshore funding channels, though the size of onshore bond issuances have been relatively small.
- **In our opinion, there are three factors which we think are important in ascertaining a developer's ability to survive.** They are: (1) its ability to generate sufficient contracted sales; (2) whether it can access onshore funding; and (3) the importance of the developer to the various local governments.
- **Based on our conversations with clients, we think that most investors, particularly those offshore, will be keeping their distance from China property developers given the huge uncertainty and volatility still lingering within the sector.** Most of our clients have pared back their exposure to China property but there is still strong interest in developers viewed to be stronger, such as Country Garden, CIFI, Sino-Ocean, and Longfor. Many are also still nursing legacy positions in distressed developers.
- **We have no Outperform recommendations in the sector at present.** For investors who are still looking for exposure to China property, we would recommend China Overseas Land (COLI, Market perform) and China Resources Land (CR Land, Market perform). Both developers are among the stronger state-linked developers thanks to their sound credit fundamentals, decent access to various funding channels, as well as their implied state support. However this is also reflected in their spreads, which are viewed as too tight by many investors when compared with other developers or state-owned Chinese credits.

## Relative Value

Please see **Asia Credit Recommendations: Sep 2022**

Chinese IG Developers: Major $ Bonds Outstanding



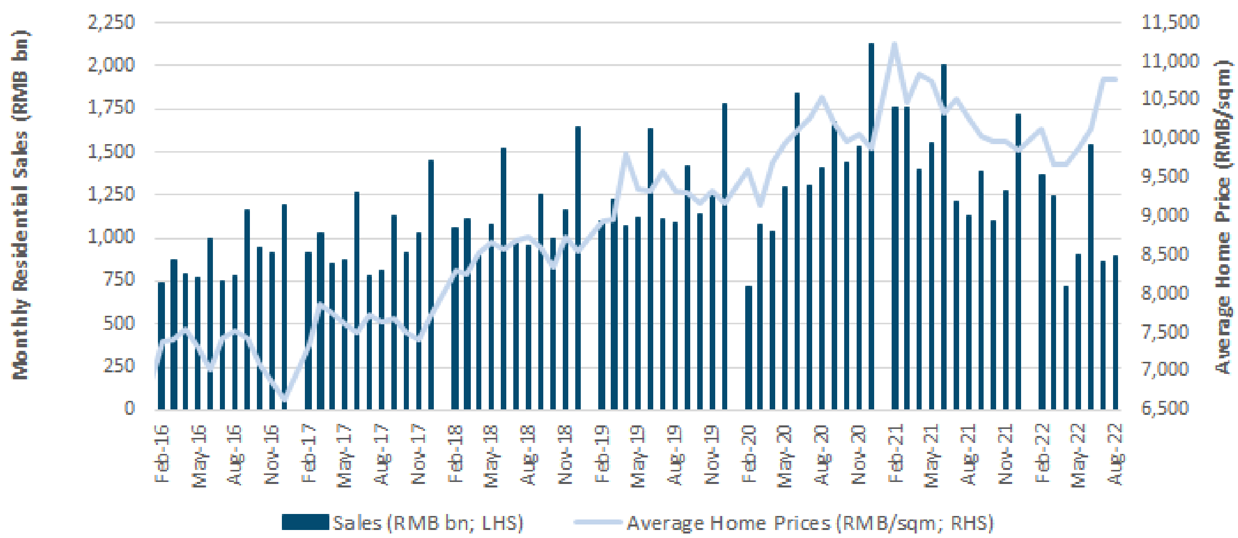

Source: Bloomberg, CreditSights. Note: Prices as at 27 September 2022, 12.42pm SGT/HKT.

**1. What are our expectations for the China property sector: will sales recover and will there be sector consolidation?**

Recent housing data released by the National Bureau Statistics of China (NBS) has shown that overall home demand still remains weak in China, as evidenced by the year-on-year decline in total home sales of 30.3% for 8M22. We expect the Chinese authorities and various local governments, particularly in the lower tier cities, to continue implementing easing housing policies in a bid to boost home demand. However, the effectiveness of such policies in inducing a rebound in home sales still remains to be seen

**China: Monthly Residential Sales & Average Home Prices**

**Total residential sales increased by 3.6% MoM in August, mainly due to a 3.6% increase in GFA sold**




Note: No data for every January. February column for first 2 months of the year.
Source: Wind Info, National Bureau of Statistics of China.

We also expect a further consolidation in the China property sector. The weaker distressed/defaulted developers may continue conducting asset disposals in an effort to raise cash to stay afloat, which will see them scaling down in size or exit the industry altogether. On the other hand, the stronger developers are likely to further consolidate their market position and capture larger a market share, as homebuyers shift towards purchasing homes from more reputable and stable developers. That said, we think that such a consolidation process will be a gradual one. Some of the stronger developers had mentioned during the recent 1H22 earnings calls that several criteria will need to be considered before engaging in any acquisitions from the weaker players.

**2. Why hasn't there been a significant recovery in home sales in China?**

Local governments across China have been introducing a myriad of easing housing policies since 3Q21. Then again, such easing measures have yet to filter through the system to effect a meaningful change and bear any significant fruit, as seen by the lackluster home sales performance year-to-date (YTD). Homebuyers are likely remaining very cautious of the China property sector, amid a growing number of defaulted developers and unfinished projects, that have weakened homebuyer confidence in the sector.

In addition, we think that the Chinese government still has an overarching mandate of "houses are for living in, not for speculation" in mind, and are keen to ensure stable home prices, land prices and market expectations. As such, we opine that the Chinese regulators may be reluctant to employ an "all-out easing" approach, lest the China property space regresses back to its old footing of runaway home prices and speculative homebuyer behaviour that the government was trying to curb in the first place.

**3. Is housing affordability deterring homebuyers in China?**

We think that the unwillingness of homebuyers to purchase homes has contributed more to the dampened home demand in China than their inability to afford a new property. Home prices, especially in the lower tier cities, have been steadily retreating. A number of cities have also been introducing a host of support measures, ranging from lowered mortgage rates to housing subsidies, in an attempt to spur home sales. However, as mentioned earlier, such measures have yet to meaningfully translate into a recovery in homebuyer confidence and home sales. Having said that, we also note that home demand in the Tier-1 cities is still relatively buoyant, as the home price index for tier-1 cities has been continuously rising YTD.

**4. How effective are the recent liquidity support measures in helping the developers?**

For many developers, conventional funding channels, such as raising new bonds or loans, have become inaccessible. Hence, most cash-strapped developers have had to resort to disposing of assets and projects to raise funds; many have also conducted debt exchange offers to buy themselves some time. While there have been some liquidity support measures, such as the **state-backed bailout fund** and the **special loans** by the policy banks, we think that the main aim of such measures is to help distressed/defaulted developers to complete and deliver their stalled projects to homebuyers, rather than to help them refinance their bonds.

On the other hand, selected developers, such as Longfor and Country Garden, have been able to tap on the onshore bond market recently via the issuance of guaranteed domestic bonds. However, the size of such bond issuances has been relatively small, ranging between RMB 1-1.5 bn: this pales in comparison to the size of their existing debt obligations. Nonetheless, we think that their ability to access the onshore bond market signals that they remain “high quality” in the eyes of the Chinese regulators and that they have likely been identified as likely survivors by the authorities.

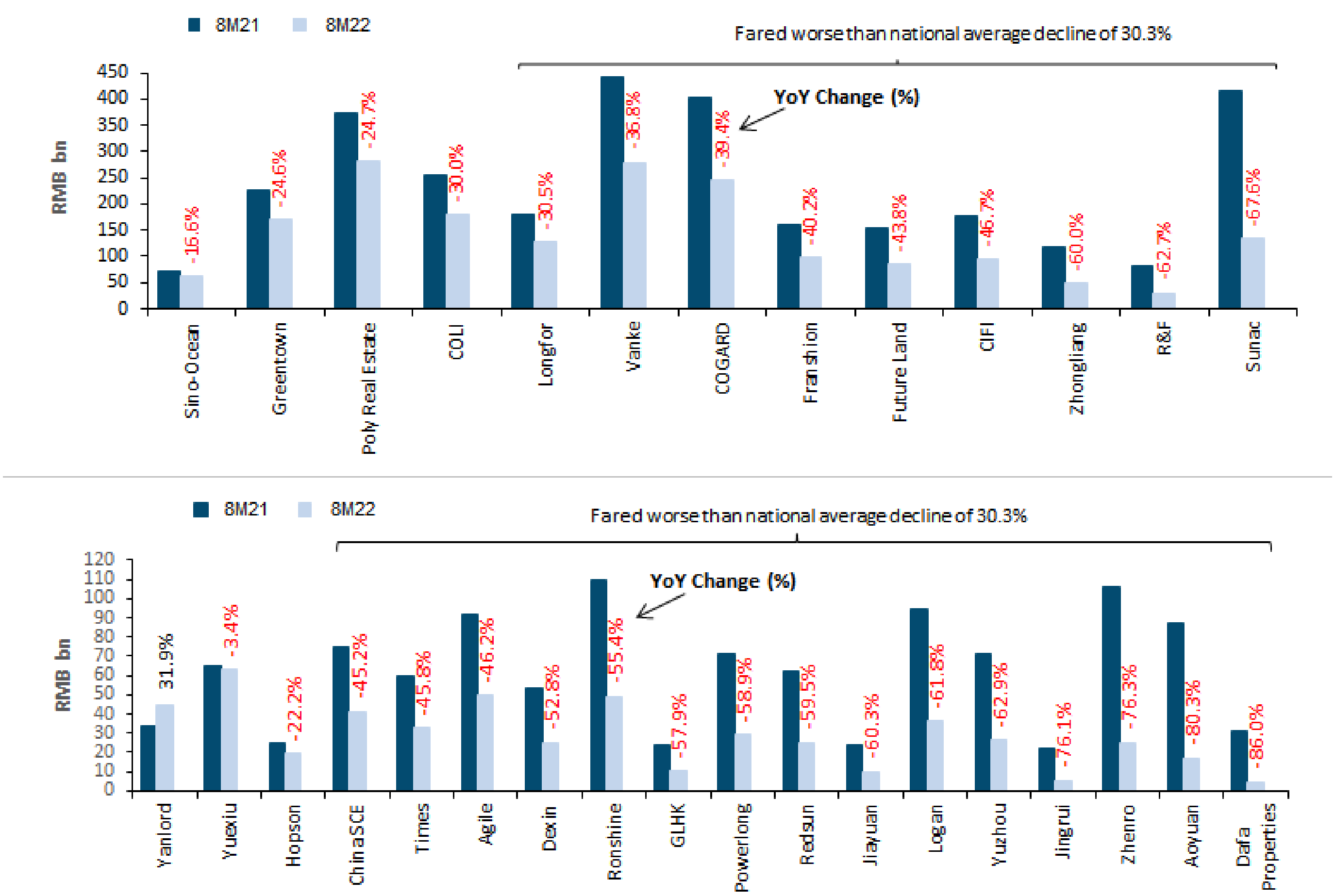
**5. What indicators should we look at to determine if a developer is able to survive?**

In our opinion, there are three factors which we think are important in ascertaining a developer’s ability to survive, namely: (1) its ability to generate sufficient contracted sales; (2) whether it can access onshore funding avenues; and (3) the importance of the developer to the various local governments.

On (1), contracted sales remain a key source of liquidity for most developers at this juncture, given that conventional funding routes have become shut to most developers. Without sufficient contracted sales, a developer’s liquidity position would become further stretched and may impair its ability to meet its operational and debt obligations. On (2), access to onshore funding channels remains a lifeline. With the offshore financing markets still largely shut to all developers, access to the onshore markets would allow developers to focus their internal resources in meeting their existing offshore debt obligations. Weaker developers which lack such onshore funding access have had to resort to alternative means instead, such as conducting asset disposals or debt exchange offers. On (3), developers of higher systemic importance to a local government are likely to receive more government support, although of course this also depends on the capacity of the local government to provide financial support.

**Chinese Property Sector: YoY Contracted Sales**

**Only Yanlord posted a YoY-increase in its 8M22 contracted sales**




Notes:

1) Agile and Greentown include the sale of property projects carrying their brand names in their gross contracted sales figure.

2) Sale of carparks are excluded from the reported contracted sales for Modern Land China (MOMA).

3) Primary land sales is excluded from the reported contracted sales for Franshion.

4) Yanlord only begin disclosing their contracted sales results in February 2020.

5) CCRE did not provide a split between its contracted sales generated from heavy assets and light assets.

6) Evergrande, Road King, Kaisa, Fantasia, MOMA, Shimao, KWG, and CR Land had not provided their Aug-22 figures at the time of publication.

Source: companies' data, CreditSights.

**6. Are offshore investors still willing to be involved in this sector?**

Most of the clients we spoke to this month have pared back their exposure to China property, save for legacy distressed positions or holdings in some of the better performing credits. "Investable" companies that investors frequently asked about included Country Garden, Longfor, CIFI, and Sino-Ocean. For the distressed names, many investors seem to be adopting a "wait and see" approach, expecting a lengthy and uncertain restructuring process ahead. Investors whose returns are benchmarked to an Asia credit index were more likely to retain holdings in the stressed, but yet to default, developers (e.g. Agile), given the risk of underperforming the index if these bonds were to suddenly recover.

**7. Which China property names do we recommend at this point?**

We have no Outperform recommendations in the sector at present given the bleak industry outlook, high refinancing risks and market volatility. However, for investors who are still looking for exposure to the China property space, we would recommend China Overseas Land (COLI, Market perform) and China Resources Land (CR Land, Market perform). Both developers are among the stronger state-linked developers thanks to their sound credit fundamentals, decent access to various funding channels and implied state support. In particular, CR Land was 59.55% effectively owned by the central SASAC according to a company filing on 22 September 2022, which makes the central government its majority shareholder. The bond prices of both developers have also been largely stable unlike some of their peers. We think that COLI and CR Land are likely to emerge as survivors from the current China property crisis.

This said, CR Land and COLI's strong credit profiles are reflected in their spreads, which are not compelling enough for several investors. Those seeking higher returns often identified Longfor and Yanlord as two of the stronger privately-run developers. Indeed, both developers are more financially prudent relative to their peers, and possess adequate liquidity as seen in their adjusted unrestricted cash (which excludes cash held in escrow accounts) to short-term debt covers as of 30 June 2022 (Longfor: 2.8x | Yanlord: 1.5x). However, we think that privately-run developers remain susceptible to rumour-mongers and short-sellers, especially if their bond prices are high. For example, Longfor experienced bouts of volatility in its bond prices in August on the back of **market rumours** alleging that it did not repay its commercial bills. As such, we are still cautious of recommending privately-run developers due to the volatility that may arise from such market rumours or short-selling activity. We currently have a Hold recommendation on both Longfor and Yanlord.

**Selected Chinese Developers: Major Bonds Outstanding**

| Issuer | Cpn | Maturity | First Call Date | Amt. Out. ($ mn) | Bond Ratings | Mid Price | T+ (bp) | Mid YTW | Rec. |
|---|---|---|---|---|---|---|---|---|---|
| COLI | 3.950% | 15-Nov-22 | Bullet | 700 | BBB+/Baa1/NR | 99.8 | 113 | 5.28% | Market perform |
| COLI | 4.250% | 26-Apr-23 | Bullet | 750 | BBB+/Baa1/A- | 99.2 | 139 | 5.70% | |
| COLI | 5.375% | 29-Oct-23 | Bullet | 500 | BBB+/Baa1/A- | 99.6 | 149 | 5.80% | |
| COLI | 5.950% | 8-May-24 | Bullet | 700 | BBB+/Baa1/A- | 100.1 | 157 | 5.89% | |
| COLI | 2.375% | 2-Mar-25 | Bullet | 300 | NR/Baa1/A- | 91.4 | 189 | 6.26% | |
| COLI | 4.750% | 26-Apr-28 | Bullet | 750 | BBB+/Baa1/A- | 90.7 | 263 | 6.77% | |
| COLI | 3.450% | 15-Jul-29 | Bullet | 450 | BBB+/NR/A- | 82.9 | 274 | 6.62% | |
| COLI | 3.050% | 27-Nov-29 | Bullet | 294 | NR/Baa1/NR | 80.0 | 273 | 6.61% | |
| COLI | 2.750% | 2-Mar-30 | Bullet | 500 | NR/Baa1/A- | 77.3 | 281 | 6.68% | |
| COLI | 6.450% | 11-Jun-34 | Bullet | 500 | BBB+/Baa1/A- | 96.4 | 302 | 6.90% | |
| COLI | 3.125% | 2-Mar-35 | Bullet | 200 | NR/Baa1/A- | 68.7 | 304 | 6.92% | |
| COLI | 5.350% | 15-Nov-42 | Bullet | 300 | BBB+/Baa1/NR | 84.9 | 271 | 6.73% | |
| COLI | 6.375% | 29-Oct-43 | Bullet | 500 | BBB+/Baa1/A- | 96.1 | 270 | 6.72% | |
| CR Land | 6.000% | 27-Feb-24 | Bullet | 700 | BBB+/Baa1/BBB+ | 100.1 | 158 | 5.89% | Market perform |
| CR Land | 3.750% | 26-Aug-24 | Bullet | 300 | BBB+/Baa1/NR | 96.1 | 162 | 5.94% | |
| CR Land | 4.125% | 26-Feb-29 | Bullet | 500 | BBB+/Baa1/NR | 89.5 | 225 | 6.13% | |
| CR Land[1] | 3.750% | Perpetual | 12-Sep-24 | 1,050 | NR/Baa2/NR | 95.1 | 186 | 6.17% | |
| CR Land (HKD Bond) [2] | 6.100% | 28-Oct-29 | Bullet | HKD 3,500 | NR/Baa1/NR | n.a. | n.a. | n.a. | n.a. |
| Longfor | 3.900% | 16-Apr-23 | Bullet | 300 | NR/Baa2/BBB | 98.8 | 187 | 6.19% | Hold |
| Longfor | 3.375% | 13-Apr-27 | Bullet | 250 | BBB-/Baa2/BBB | 78.4 | 517 | 9.32% | |
| Longfor | 4.500% | 16-Jan-28 | Bullet | 500 | NR/Baa2/BBB | 78.6 | 563 | 9.77% | |
| Longfor | 3.950% | 16-Sep-29 | Bullet | 850 | BBB-/Baa2/BBB | 73.3 | 536 | 9.24% | |
| Longfor | 3.850% | 13-Jan-32 | Bullet | 400 | BBB-/Baa2/BBB | 70.6 | 461 | 8.48% | |
| Yanlord | 6.750% | 23-Apr-23 | 23-Apr-21 | 350 | B+/Ba3/NR | 96.3 | 949 | 13.80% | Hold |
| Yanlord | 6.800% | 27-Feb-24 | 27-Feb-22 | 400 | B+/Ba3/NR | 89.0 | 1,149 | 15.80% | |
| Yanlord (Green) | 5.125% | 20-May-26 | 20-May-24 | 500 | NR/Ba3/NR | 73.8 | 1,053 | 14.68% | |

Note 1: Subordinated perp with step-up coupon of 300 bp if not called on first call date
Note 2: No indicative pricing for CR Land's HKD bond.
Source: Bloomberg, CreditSights. Note: Prices as at 27 September 2022, 12.42pm SGT/HKT.

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## RELATED COMPANIES

| | | |
|---|---|---|
| HOLD Agile Group | M/P China Overseas Land | M/P China Resources Land |
| HOLD Country Garden | N/R Evergrande Group | N/R Kaisa Group |
| HOLD KWG Group | HOLD Longfor Group | N/R Powerlong Real Estate |
| SELL Road King Infrastructure | | |

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