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Flash note
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Daily follow-up of the Evergrande saga (and Chinese HY)

- First signs of public support for real estate companies in China: The Chinese city Harbin becomes first city to announce steps to support property developers, by directly supporting projects that are already under construction by property developers. In addition, it was announced that cash held in escrow accounts will be returned as quickly as possible while developers with good credit records should be allowed to restart presale activities. Other cities are expected to follow suit.
- Meanwhile, Evergrande contagion remains as a potential trigger for a wave of defaults in other developers, according to a distressed debt specialist, Michel Lowy, who told Bloomberg that property firms now face a triple threat: 1) Dwindling access to offshore financing, 2) "catastrophic" September pre-sales, and 3) a limited onshore banking market. According to the expert, the three aspects are combining to create the potential for a large wave of defaults in the coming months if conditions don't ease for heavily indebted borrowers. Fears of contagion risks intensified last week after a surprise default by Fantasia Holdings Group Co. spurred a dramatic selloff in the offshore market that sent yields on China dollar junk bonds to 16.9%, the highest in about a decade, while Evergrande's dollar bond prices sank to a record low.

The obvious risk is that the increase in yields becomes indiscriminate in Chinese Junk Bonds and makes it near-impossible for developers to refinance maturing debt. Sales of new USD debt from high-yield or unrated property firms during this third quarter fell to their lowest since late 2017. An important issue since such companies need to refinance or repay some $5.3 billion of outstanding dollar bonds maturing the rest of this year, followed by $10.1 billion in the first quarter of 2022. Ultimately, it's a liquidity game. At the moment stress levels have been rising in September in both the local and offshore Chinese corporate bond markets (with a size of US$12trn).

Last week we decided to sell our entire position in Chinese HY bonds, considering that during the next two months these bonds would not have market support or the necessary triggers to see a rapid turn in prices, while still having the potential to expose portfolios to additional los

Best