联合评级国际
Lianhe Ratings Global

Non-Rating Commentary
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China Offshore Bond Market 1H2021 Review and 2H2021 Outlook: Intensified Polarization Amid Tightened Financing Environment

Summary

China offshore USD bond new issuance amount showed a slight rebound of 5.0% year-on-year in 1H2021, but the amount was still lower than those in 2H2020 and 1H2019. The majority of the new issuance amount (72%) was related to bonds with maturity of 1-5 years. At end-1H2021, 32% of the total outstanding amount will mature on or before end-2022, so we expect the refinancing demand remains intact going into 2H2021.

The real estate offshore USD bond issuance dropped by 10.2% in 1H2021. The issuance was supported by the refinancing demand, but dampened by the credit events of developers. China's nationwide contracted sales recorded a strong growth of 38.9% in 1H2021. However, land replenishment remained subdued given developers' prudent deleveraging approach and the centralized land supply policy. We expect the policy headwinds will continue in 2H2021, with the purpose of reining in the robust property price growth.

In regard to LGFV, the fiscal conditions weakened for most of the provinces in 2020, given the higher expenditures and debt for the counter-cyclical measures to counter decline in GDP and fiscal income. Local governments were required to strengthen their debt managements. The proposed centralized land sales revenue collection policy will make local governments less flexible in their fiscal conditions. However, LGFVs' offshore USD bond issuance increased by 5.7% in 1H2021, with the proceeds mainly used for refinancing.

Green and sustainable bonds are becoming an asset class well accepted by institutional investors. There were 27 Chinese offshore green and sustainable issuance in 1H2021, which already exceeded the total 18 issuances for 2020. The Hong Kong government provides subsidy for eligible bond issuers and loan borrowers to cover their expenses on bond issuances and external transaction-related review costs.

In 2H2021, we expect the financing environment remains challenging for both Chinese property developers and LGFVs. The stringent regulations and measures will intensify credit polarization of issuers' financial positions. Also, the risk aversion stance in the offshore bond market may favor IG issuers. Under the regulatory requirements, we anticipate the new issuance will be mainly driven by the demand for refinancing. The rising inflation expectation and currency risk will be the major macro risks.

For the property market, we expect nationwide contracted sales momentum will sustain, but the growth rate will slow down and normalize. Developers will continue deleveraging and striving to diversify land acquisition methods away from the open market auctions. For LGFVs, we expect their issuance volume to slightly pick up in 2H2021, driven by the refinancing demand. There will be a higher degree of delineation or refinement between LGFVs and local governments debt. This will lead to a higher degree of credit polarization in which regions and provinces with high level of implicit debt will likely face refinancing hurdles.

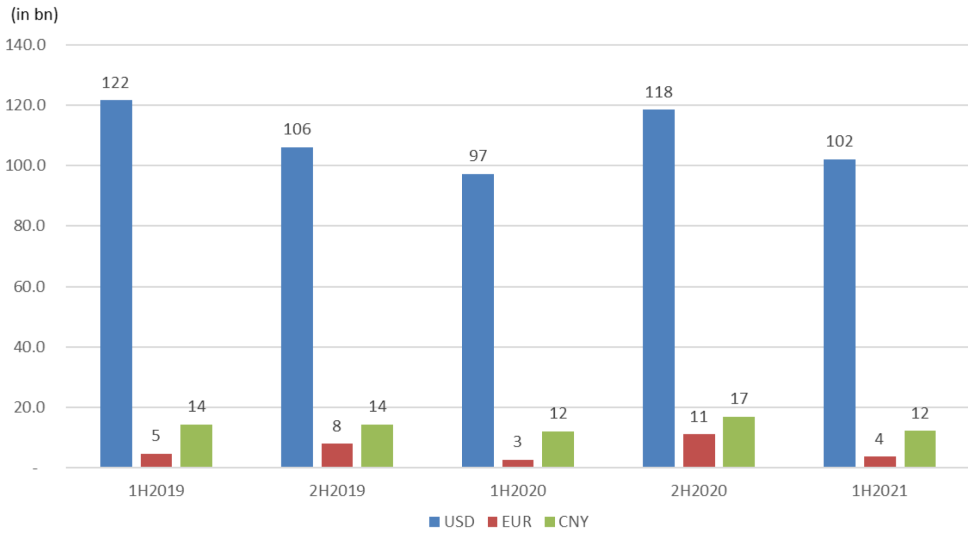
1. Review of China Offshore USD Bond Market in 1H2021

New Issuance Rebounded Slightly Year-on-year

China offshore USD bond new issuance reached USD102 billion in the first half of 2021 (1H2021) (EXHIBIT 1), showing a year-on-year growth of 5.0% compared with the trough in 1H2020. However, the amount was lower than 2H2020 and 1H2019 by 13.8% and 16.0%, respectively. There were 322 new issues in 1H2021 (EXHIBIT 2), compared with 283 new issues in 1H2020.

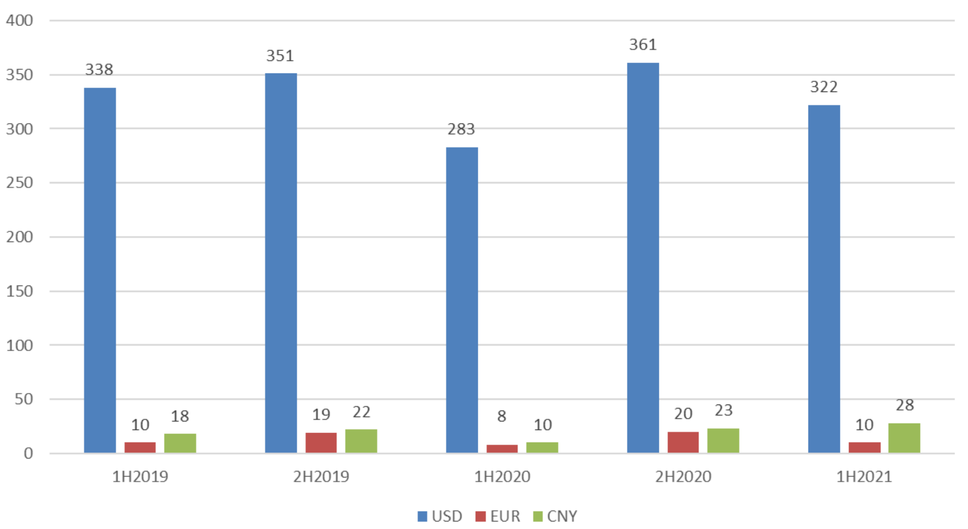
On a monthly basis, the refinancing need of Chinese property developers supported the bond issuance in January. However, the rise of US treasury yield, the Chinese New Year holiday and the credit event of China Fortune Land Development Co., Ltd. ("CFLD") resulted in the decline in the bond issuance in February and March. The issuance amount remained roughly stable throughout the second quarter of 2021.

Exhibit 1: Total Amount of China Offshore Bond New Issuance



Source: Bloomberg and Lianhe Global's calculation

Exhibit 2: Number of China Offshore Bond New Issuance



Source: Bloomberg and Lianhe Global's calculation

Rising Trend of Short Tenor Issuance

In terms of tenor, bonds with maturity of 1-5 years accounted for 72% of the total USD issuance amount in 1H2021 (EXHIBIT 3). Short-term bonds with maturity of less than 1 year became more popular and contributed 9% of the total USD issuance in 1H2021. Bonds with maturity of 3-5 years accounted for 32% of the total issuance in 1H2021, followed by bonds with maturity of 1-3 years (31%).

At end-1H2021, the outstanding amount of offshore USD bond was USD787 billion. USD252 billion will mature in either 2H2021 or 2022, which accounted for 32% of the total outstanding amount (EXHIBIT 4). Therefore, we expect the refinancing demand from issuers remains intact and it will support the new issuance going into 2H2021, especially for LGFVs.

Exhibit 3: Tenor Distribution of China Offshore USD Bond New Issuance in 1H2021

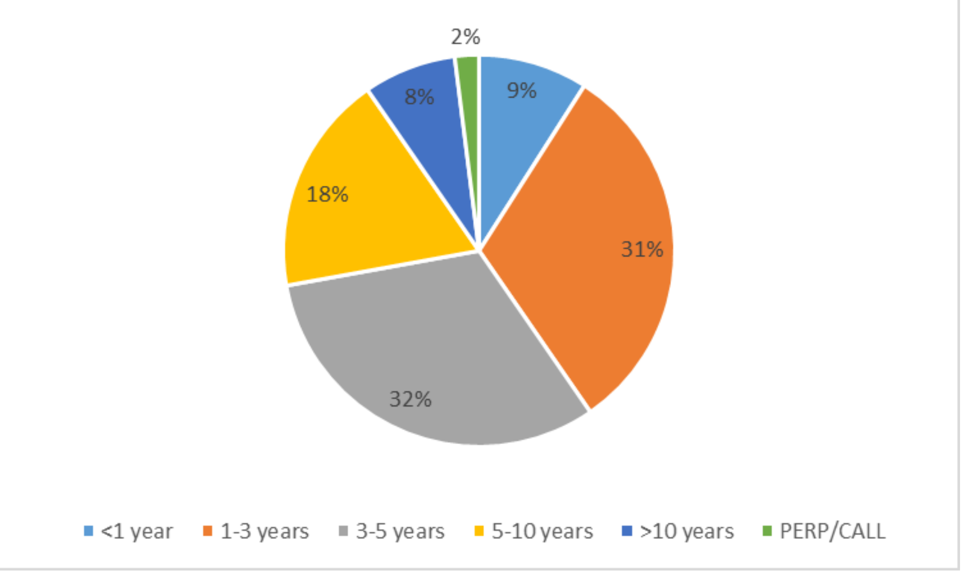
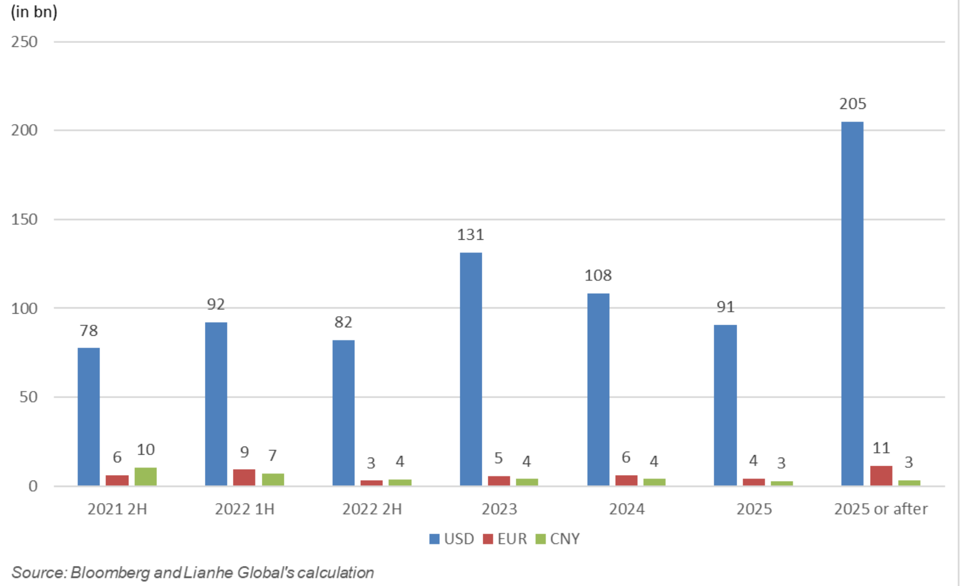


Exhibit 4: Maturity Distribution of China Offshore Bond at end-1H2021



Source: Bloomberg and Lianhe Global's calculation

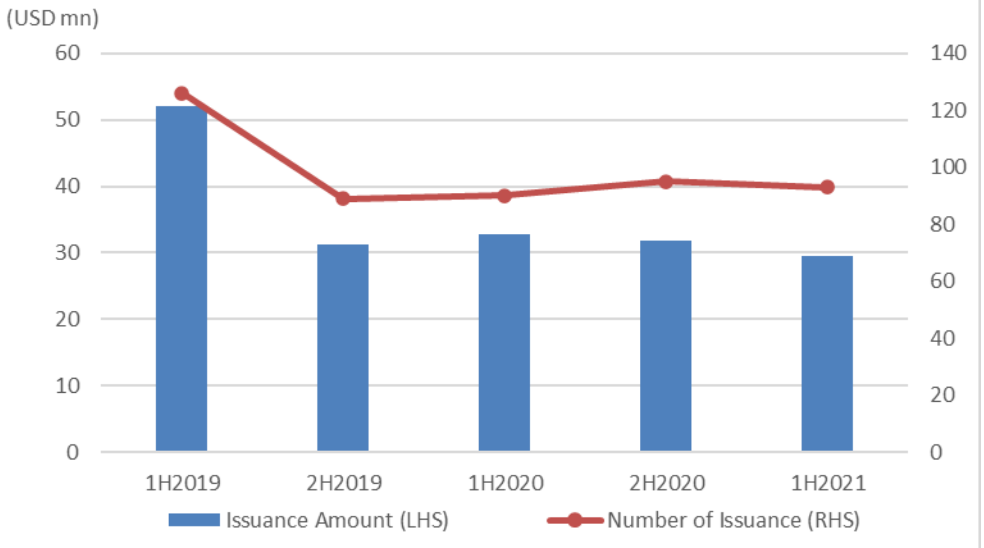
2. Review of China's Property Market in 1H2021

Real Estate Offshore USD Bond Issuance Dropped in 1H2021

China real estate offshore USD bond issuance reached the peak in January, supported by the refinancing demand driven by the maturity tower in 1H2021, continuous USD depreciation against RMB and the global loosing monetary policies. Given the stringent onshore regulatory and financing environment, developers were eager to utilize their offshore financing channels. However, investors' sentiment has been dampened by the credit event of CFLD and the tightening policies on both property market and onshore financing channel since February.

As such, the issuance amount of China real estate offshore USD bond dropped by 10.2% year-on-year to reach USD29.5 billion in 1H2021 (EXHIBIT 5). Also, the amount was lower than 2H2020 and 1H2019 by 7.7% and 43.4%, respectively. The real estate bonds contributed 29% of the total offshore USD issuance in 1H2021 (1H2020: 34%).

Exhibit 5: Offshore Real Estate USD Bond Issuance Amount and Number of Issuance



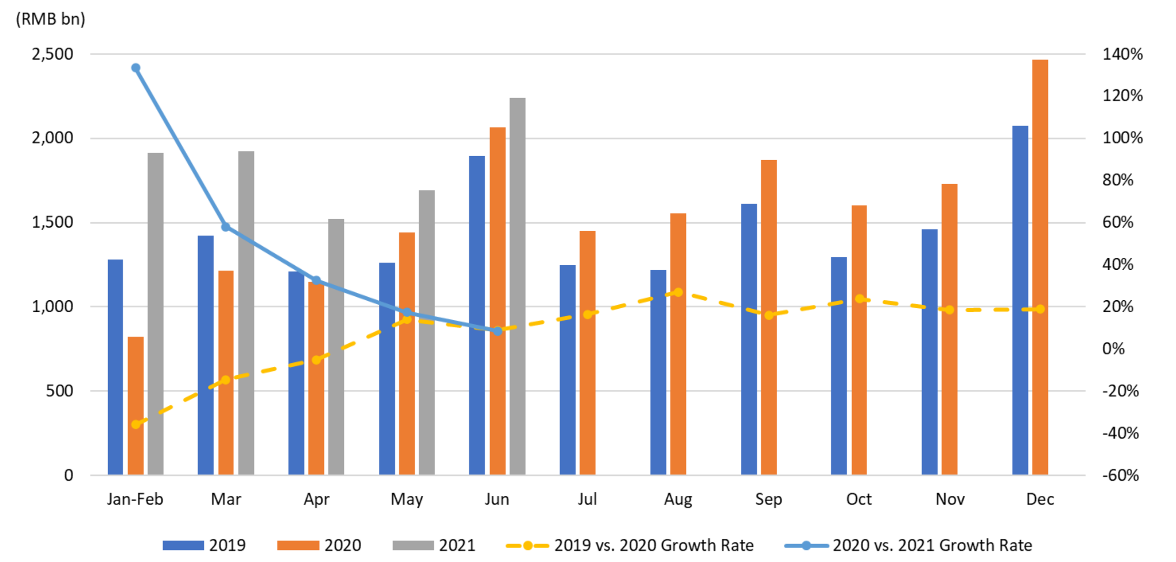
Source: Bloomberg and Lianhe Global's calculation

Strong Contracted Sales Momentum

China's contracted sales demonstrated strong growth momentum in 1H2021, driven by the steady demand and the decreasing inventories. According to the National Bureau of Statistics, the total contracted sales and GFA surged 38.9% and 27.7% year-on-year in 1H2021, respectively. If the data is compared with the same period in 2019, which excludes the low base impact from the coronavirus outbreak ("COVID-19") in 1H2020, the growth rate for contracted sales and GFA remained healthy at 31.4% and 17.0%, respectively.

Lianhe Global's rated Chinese property entities recorded even higher contracted sales growth of 58.5% year-on-year on average for 1H2021 (EXHIBIT 7). If the data is compared with the same period in 2019, the growth remained strong at 60.5%. Their contracted sales were on track as they achieved 51.4% of their full-year targets on average in 1H2021.

Exhibit 6: Monthly Contracted Sales Amount and Year-on-year Change



Source: National Bureau of Statistics of China, Lianhe Global's calculations

Exhibit 7: Lianhe Global's Rated Chinese Property Developers' 1H2021 Contracted Sales

Issuers name	Contracted Sales			Change	
	1H2021 (RMB bn)	1H2020 (RMB bn)	1H2019 (RMB bn)	1H2021 vs 1H2020	1H2021 vs 1H2019
Agile Group Holdings Limited ("Agile")	75.3	55.1	58.2	36.7%	29.4%
China Aoyuan Group Limited ("Aoyuan")	67.6	50.9	53.6	32.8%	26.0%
CIFI Holdings (Group) Co. Ltd. ("CIFI")	136.2	80.7	88.4	68.6%	53.9%
Dexin China Holdings Company Limited ("Dexin")	43.0	25.7	21.8	67.4%	97.2%
Jiangsu Zhongnan Construction Group Co., Ltd. ("Zhongnan")	109.0	81.4	81.2	33.9%	34.2%
Jingrui Holdings Limited ("Jingrui")	18.7	7.7	10.1	144.3%	84.8%
Jinke Property Group Co., Ltd. ("Jinke")	102.1	86.8	81.4	17.6%	25.4%
Logan Group Company Limited ("Logan")	73.6	46.4	45.3	58.9%	62.5%
Redco Properties Group Limited ("Redco")	23.5	13.0	10.9	80.6%	115.5%
Redsun Properties Group Limited ("Redsun")	49.2	31.6	30.3	55.7%	62.5%
Sinic Holdings (Group) Company Limited ("Sinic")	58.8	43.5	N/A	35.0%	N/A
Yango Group Co., Ltd. ("Yango")	101.3	90.0	90.1	12.6%	12.5%
Yincheng International Holding Co., Ltd. ("Yincheng")	16.5	6.1	7.9	170.1%	109.3%

Yuzhou Group Holdings Company Limited ("Yuzhou")	52.7	42.9	28.5	23.0%	85.1%
Zhongliang Holdings Group Company Limited ("Zhongliang")	95.0	67.7	63.7	40.3%	49.1%
Average:				**58.5%**	**60.5%**

Note:
- Simple average is applied for the change of 1H2021 versus 1H2020 and 1H2021 versus 1H2019.
- Developers with public announcement of comparable contracted sales data are included in this exhibit.
Source: Issuers' announcements, Lianhe Global's calculations

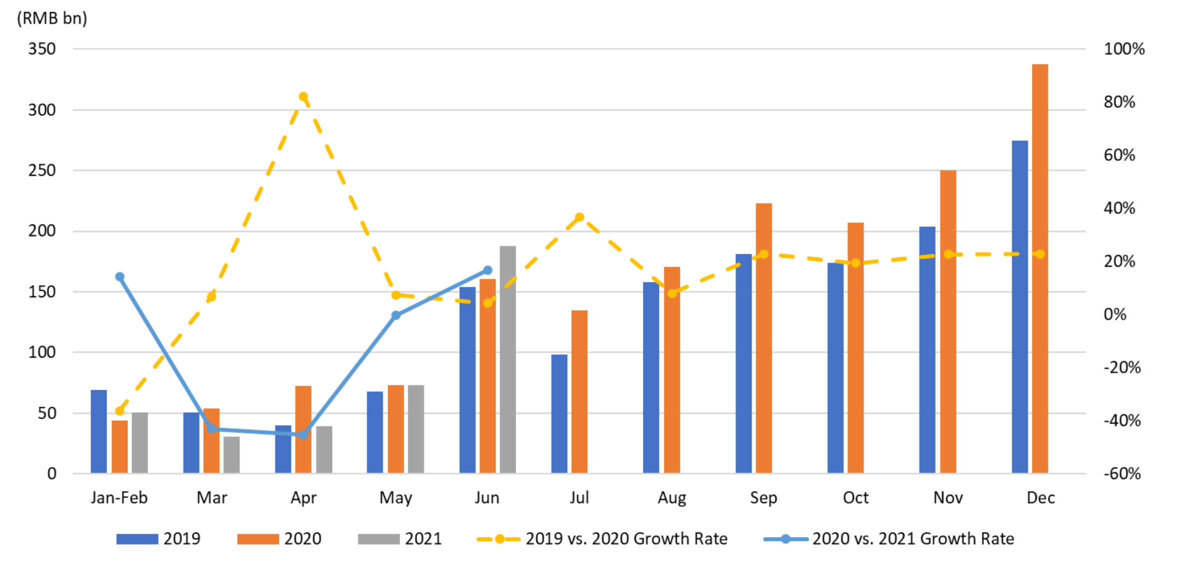
Land Purchase Dropped due to Developers' Deleveraging and Centralized Land Supply

The centralized land supply policy was introduced and implemented in 22 key cities in 1H2021. These cities are required to limit the number of residential land sales to thrice a year, and raise the residential land supply for each auction. The government aims to stabilize the land price through this scheme, and eventually ease the upward pressure of residential property prices. As of the end of June, most of these 22 cities completed the first batch of land auction.

Developers generally remained prudent on land acquisition in 1H2021, given their priority on deleveraging and meeting the "3 Red Lines" rule over scale expansion. Also, developers adopted "wait-and-see" attitude towards the centralized land supply policy. As such, according to the National Bureau of Statistics, China's land purchase volume dropped 11.8% year-on-year in 1H2021, and the land purchase amount decreased by 5.7% during the same period.

However, the competition for land parcels in major cities remains fierce. Given the developers' need for land bank replenishment driven by strong contracted sales, and two out of the three batches of land sales are scheduled in 2H2021 for most of the cities adopting the centralized land supply policy, we expect the land market to stabilize going to 2H2021.

Exhibit 8: Monthly Land Purchase Amount and Year-on-year Change

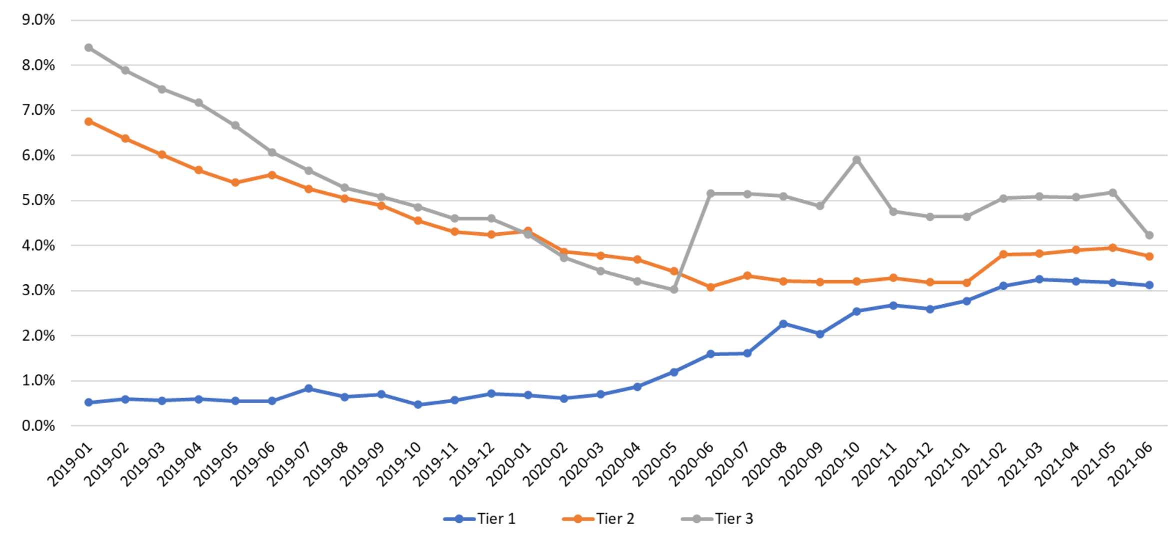


Source: National Bureau of Statistics of China, Lianhe Global's calculations

Policy Headwinds to Restrain Robust Property Price Growth

China's home price maintained the uptrend in 1H2021. Prices in tier 1 and 2 cities were supported by the strong contracted sales, accelerating urbanization and limited supply in prime locations, but the extent of price increase was limited by the price restrictions and other restrictive policies. On the other hand, some developers explored opportunities in some tier 3 cities with good potential, benefiting from the spillover demand from neighboring tier 1 and 2 cities and higher profit margin driven by the lower land cost.

Exhibit 9: Year-on-year Growth Rate of Home Price in 100 Major Cities



Source: WIND, Lianhe Global's calculations

The "3 Red Lines" rule was introduced in August 2020. While no official implementation is announced, developers are voluntarily focusing on deleveraging and complying with the relevant requirements. With reference to the 2020 annual results, most of Lianhe Global's rated Chinese property entities were able to pass 2 out of the 3 thresholds, namely net gearing ratio and cash/short-term debt ratio, at end-2020. These developers target fulfilling the remaining requirement, namely liability-to-asset ratio, either at end-2021 or end-2022.

At the beginning of 2021, banks are required to comply with the maximum caps of 40% and 32.5% for outstanding property loans and mortgage loans to their total loans, respectively. We believe this policy limits banks' exposure to the property sector and tightened the loan supply to both developers and mortgage buyers in the long term. In 1H2021, banks have tightened their mortgage policies, including: i) raising the mortgage rate on both first-home and second-home purchase, ii) lengthening the approval of mortgage loan application to over 3 to 6 months, and iii) scrutinizing the funding source of down-payment. We expect these policies undermine the purchasing power of mortgage buyers and developers' liquidity generating from contracted sales. These policies also help to prevent the illegal flow of funds from consumption and business loans to the property purchase.

In some cities such as Shenzhen, the reference price mechanism was imposed on its secondary market. The reference price is released by the local government, and it is usually lower than the market price. Thus, this mechanism would squeeze the mortgage loan amount granted by banks, and mortgage buyers probably need to pay a higher proportion of down-payment. Together with the centralized land supply policy as previously mentioned, we believe the central government is concerned about the risk of continuous increase in property price and potential overheated property price in some cities. Therefore, we anticipate the strict policy stance will continue in 2H2021, until there is any signal of stabilizing property prices.

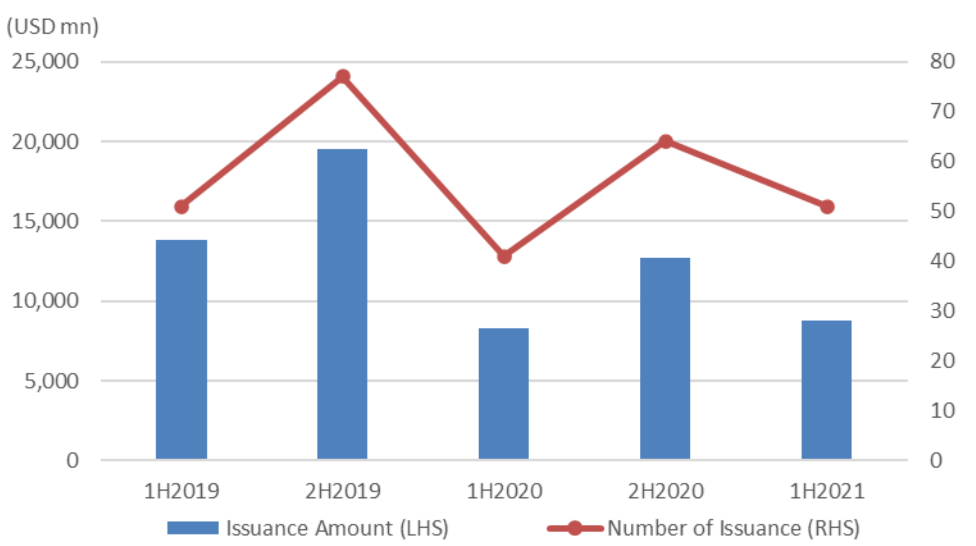
3. Review of LGFVs in 1H2021

LGFVs' Offshore USD Bond Issuance Rebounded but Remained Restrained in 1H2021

LGFVs went through a rough patch in 1H2021 with subdued issuance as a result of the spillover effect of the changing investor sentiments from a spate of SOE defaults. With the rebound of the Chinese economic growth, the need for refinancing and relatively more favorable financing cost offshore, the issuance amount of China LGFVs' offshore USD bond reached USD8.7 billion in 1H2021 (EXHIBIT 10). While this amount represented a year-on-year increase of 5.7% compared with the trough in 1H2020, it was still lower than 2H2020 and 1H2019 by 31.3% and 36.7%, respectively. Under the regulatory requirements, issuance was mainly used for refinancing LGFVs' offshore debt instead of new financings.

The Chinese government has urged local governments to strengthen their debt managements, such as strictly controlling and resolving the risk of implicit debt, improving the efficiency of the use of fund from financing, and reinforcing the management of specialty debt, etc. Moreover, LGFVs are prohibited from raising new debt and repaying the implicit debt for local governments. According to the Ministry of Finance, total new bond issuances by local governments showed a year-on-year decrease of 20.4% to RMB2,546.3 billion for 5M2021, compared with RMB3,199.7 billion for 5M2020.

Exhibit 10: Offshore LGFV USD Bond Issuance Amount and Number of Issuance



Source: Bloomberg and Lianhe Global's calculation

Polarization of Fiscal Conditions and Advocate of Self-sustainability

At end-2020, local government outstanding debt reached RMB25.49 trillion. There were 9 provincial governments with outstanding debt over RMB1 trillion. Most of the provincial governments' debt annual growth stayed in the range of 10-30% with manageable debt servicing capacity. Provinces with higher debt growth rate were generally those with higher debt servicing capacity. On the other hand, most of the provinces recorded increase in debt ratio (total debt over budgetary fiscal income and over GDP) in 2020, given the increase of debt from the counter-cyclical measures, together with the decline in GDP and fiscal income amid the COVID-19.

Provinces in eastern China with well-developed economies generally recorded higher broad-based outstanding debt (sum of local government's outstanding debt and LGFVs' interest-bearing debt), due to the larger number of LGFVs and the higher amount of LGFVs' debt in these provinces. For example, Jiangsu province's broad-based debt exceeded RMB8 trillion at end-2020, followed by Zhejiang, Shandong and Guangdong provinces. LGFVs' debt accounted for 50-70% of the total broad-based debt in these provinces. However, given the support from strong local economic performance and local governments' fiscal conditions, these local governments enjoyed wider access of funding channels and lower financing costs.

On the contrary, less-developed provinces in northwestern, northeastern and southwestern China faced higher repayment burden. These local governments had higher debt balance compared with their fiscal income. For example, Qinghai province and Inner Mongolia autonomous region recorded high debt ratio at end-2020, due to their slow GDP growth of 1.5% and 0.2%, respectively. Guizhou and Gansu provinces also recorded high debt ratio at end-2020. Therefore, they had limited room for issuing new debt and their fiscal conditions remained tight.

28 out of 31 provinces recorded slower growth rates of broad-based outstanding debt than that of local government debt in 2020. It shows that some of the LGFVs debt is gradually being replaced by local governments debt, and the proportion of local governments debt to the broad-based outstanding debt is becoming more explicit. Local governments are required to control their debt growth and strengthen their debt servicing capacity, whereby their budgetary fiscal income should be adequate to support or even exceed the principal and interest payments burden during the same period.

Generally speaking, the creditworthiness in terms of probability of support is generally higher for LGFVs under sponsor governments at higher administrative levels, such as direct-administered municipalities, cities specifically designated in the state plan and provincial capitals, given the i) inherently more important roles they play in supporting China's development, ii) their relatively stronger economic fundamentals, and iii) the potential implications and impact they may bring should adverse credit events occur.

Centralized Land Sales Revenue Collection Undermines Fiscal Flexibility

In June 2021, the Ministry of Finance issued a notice requiring the collection of four types of local governments' income, including revenue from land sales, to be transferred from local natural resource department to the central tax authorities. The policy will be applied in seven pilot provinces and municipalities in July, followed by nationwide implementation starting from 2022.

Under this new policy, local governments still retain the ownership of the land sales revenue. However, given the revenue from land sales contributes a significant portion of local governments' fiscal income, the centralized revenue collection policy will make local governments less flexible in their fiscal conditions, such as matching the income and expenditure schedules. As such, we expect the local governments will be more prudent in budgeting their expenditures.

4. Green and Sustainable Bonds

For the past ten years, green and sustainable bonds have been developed to address the global climate change, and are becoming an asset class well accepted by institutional investors. There were 27 Chinese offshore green and sustainable issuances for the first half of 2021, which already exceeded the total 18 issuances for 2020. The 27 offshore issuance comprises USD7.8 billion (24 issuances), EUR1.6 billion (2 issuances) and CNH208 million (one issuance).

Many market participants believe that China zero carbon policy continues attracting more green bond issuances and more international funds investing in Chinese offshore green bonds. Chinese property developers have been establishing their green and sustainable financing frameworks, which detail the use of proceeds for eligible green projects, green project evaluation and selection, management of green issuance proceeds, and proceed allocation reporting, to guide the Chinese property industry towards sustainability. Our rated green and sustainable bonds and notes issued by Chinese property developers include Agile Group Holdings Limited, CIFI Holdings (Group) Co. Ltd., Redco Properties Group Limited, Redsun Properties Group Limited, Shinsun Holdings (Group) Co., Ltd. and Sinic Holdings (Group) Company Limited.

Green and sustainable offshore bonds mostly solicit external reviews to certify their compliance with green bond standards. One commonly-applied green bond standard is the Green Bond Principles (GBP) of the International Capital Market Association (ICMA). With the external certification, Chinese offshore green and sustainable bond issuers can easily draw the attention of international ESG-focused investors. The most active green certification service providers include, but are not limited to, Sustainalytics, an active ESG rating and research company acquired by Morningstar in 2020, and Hong Kong Quality Assurance Agency (HKQAA), a local government-supported company in Hong Kong.

Some countries and regions give a lot of support in developing the green and sustainable bond markets. For example, the Hong Kong Government Green and Sustainable finance grant scheme, which commenced in May 2021, provides subsidy for eligible bond issuers and loan borrowers, which include Chinese offshore green and sustainable bond issuers, to cover their expenses on bond issuances (for eligible first time green and sustainable bond issuers) and external transaction-related review costs.

5. Major Credit Events in 1H2021

CFLD once a top 20 property developer by contracted sales in China announced its first missed onshore bank and trust loan principal and interest payments in early February 2021, followed by its second missed principal and interest payments including offshore bonds in late February 2021. CFLD first experienced distress as early as 2018 when it reported a dramatic drop in its cash collection rate to 45%-50% from its contracted sales as a result of an untimely expansion outside the pan-Beijing area when it was hit by a series of draconian policy measures in the region. CFLD also experienced working capital constraints as a result of long government reimbursement periods for its completed industrial park infrastructure projects including primary land development. In 2020, CFLD received another blow from the COVID-19 outbreak with an over 50% drop in its total contracted sales. CFLD's total contracted sales ranking dropped to 47th place in 2020 from 20th in 2019, according to China Real Estate Information Corporation. Based on Bloomberg's information, Ping An Life Insurance Company of China, Ltd. has a 25% equity stake in CFLD at end-June 2021. According to Bloomberg, CFLD's USD notes due January 2025 dropped to 37 cents on the dollar in mid-July, the worst drop ever, indicating a low recovery rate.

China Evergrande Group ("Evergrande"), one of the most indebted Chinese property developers, has been put under scrutiny since 2017 when the deleveraging campaign started. Evergrande is one of the top 3 property developers in China and once a prolific issuer in the offshore USD bond market with reported total borrowings amounting to RMB716.5 billion at end-2020. Evergrande is also one of the twelve property developers put under a pilot scheme of the "3 Red Lines" rule. At end-2020, Evergrande failed all three tests at end-2020. Evergrande faces a tall order to reduce its debt via debt reduction, asset disposals, as well as spinoff or listing of noncore subsidiaries to shore up its balance sheet. Evergrande had RMB158.8 billion of cash against short-term borrowings of RMB335.5 billion (47% of the total borrowings) at end-2020. In early June 2021, it was reported that China's regulators asked Evergrande's lenders to conduct stress tests on their exposure to the most indebted property developer. This unsettling news rattled the bond markets. The notion of "Too Big To Fail" is being re-examined.

China Huarong Asset Management Company ("Huarong"), one of China's big four state-owned asset management companies, announced on 1 April 2021 that it would delay in releasing its 2020 results because its auditor was not able to finalize a transaction. On the same day, its stock was suspended from trading in Hong Kong. As a state-owned enterprise ("SOE"), Huarong is perceived to have government support in time of need. Huarong has about USD20 billion of offshore notes outstanding at end-2020. Despite news reports of restructuring and withholding of bank loans etc, Huarong has made good on all of its onshore and offshore bonds so far. But some investors started to have doubts about these so-called strategically or systemically important SOEs. The implication of a perceived weaker link between the sovereign and the SOE runs deep and wide.

Sichuan Languang Development Co. Ltd. ("Languang") once a leading property developer focusing on tier 2 and 3 cities and the Chengdu region now faces a downward spiral since early 2021 due to its reliance on nonbank financing. The developer has started to expand into higher-tier cities since 2015 and it has relied on short-term and nonbank financing such as trust loans to fund its expansion. In May 2021, Languang first experienced stress as a result of cash proceeds from its contracted sales being held at the project company level for construction. Languang defaulted on its onshore debts in mid-July which likely trigger cross-default provisions on the offshore USD bonds. Languang has USD1.05 billion of USD bonds outstanding at end-June 2021, according to Bloomberg.

Lianhe Global does not have any ratings on the aforementioned companies in this section.

6. Outlook on 2H2021

Developers' Strategies – Moderate Contracted Sales Growth, Continuous Deleveraging and Diversified Land Acquisition Methods

Developers are generally optimistic on their contracted sales outlook for 2H2021, with the full-year growth target of 10-15% on average for 2021. They focus on higher-tier cities and some tier 3 cities with good potential as the major sources of their contracted sales. However, we expect the growth of contracted sales and ASP will slow down and normalize going into 2H2021, given: i) more restrictive policies in place, especially in tier 1 and 2 cities, ii) tighter liquidity and monetary policies, and iii) higher comparable base as China's property market has recovered gradually since 2Q2020. On the other hand, we anticipate the demand in tier 1 and 2 cities remains strong and continues to support the uptrend of contracted sales. Overall, we forecast the contracted sales to grow by c. 10-15% in 2021.

Developers are paying more attention to deleveraging and are generally cautious about their total debt growth. Most of them plan a modest growth (i.e. less than 10%), flat or even a slight decline of total debt in the next 1 to 2 years. We expect the deleveraging trend will continue in 2H2021, with most of the developers to record a decline in net gearing ratio. As mentioned above, most of Lianhe Global's rated Chinese property entities target fulfilling all of the three thresholds under the "3 Red Lines" rule either at end-2021 or end-2022.

Developers strive to diversify their land acquisition methods away from the open market auctions. For example, many developers resort to urban renewal projects (URPs) for acquiring valuable land at reasonable costs, despite taking the risk of uncertain and lengthy redevelopment pace. Also, developers employ joint ventures, associates and minority interests in land acquisitions, which help to lower their need of capital in the initial stages but probably increase their off-balance sheet debt.

LGFVs' Issuance Influenced by Divergence of Local Governments' Fiscal Conditions

Given the need to refinance their maturing bonds, we expect LGFVs bond issuance to slightly pick up in 2H2021. With the divergence in fiscal conditions and economic performance across provinces and regions, coupled with the central government's initiative to differentiate state support given to LGFVs, credit polarization is expected to continue in 2H2021.

Regions with stronger fundamental economic and fiscal environment will likely maintain their slight outstanding debt growth. Also, provinces with moderate economic development will probably have higher debt growth compared with provinces in western China. In comparison, the fiscally weaker provinces will have to demonstrate an accelerated progress in replacing LGFVs debt with local governments debt.

In addition, LGFVs with the main operations in carrying core policy functions will likely continue to enjoy higher probability of support from their sponsor governments and to be more favored by investors. On the other hand, LGFVs with business steering away from policy role and to "less-preferred" commercial operations such as those in the over-capacity industries will likely face more challenges ahead in maintaining a good visibility for government support.

Going forward, there will be a higher degree of delineation or refinement between LGFVs and local governments debt. This will lead to a higher degree of credit polarization in which regions and provinces with high level of implicit debt will likely face refinancing hurdles. These local governments need to slow down their debt growth and control their implicit debt via means such as consolidation of small and less critical LGFVs and debt restructuring. We are cautious on regions with high leverage but weak debt servicing capacity and LGFVs who play less important roles in carrying core policy functions for their governments.

Intensified Credit Polarization, New Issuance Driven by Refinancing

The offshore bond financing environment will remain challenging for both Chinese property developers and LGFVs. Both developers and LGFVs are restricted to issuing new bonds other than for the purpose of refinancing their offshore indebtedness maturing within one year under the No. 778 Announcement (for developers) and No. 666 Announcement (for LGFVs). As seen in EXHIBIT 4, the outstanding amount of offshore USD bond maturing in 2H2021 and 2022 reached USD252 billion at end-1H2021. Also, some of the bonds are puttable which enable the bondholders to demand early repayments. This will also potentially increase the refinancing burden of issuers. As such, we anticipate that new issuance will be mainly driven by the demand for refinancing going into 2H2021.

The central government is determined to control and strengthen the financial positions of property developers, LGFVs and local governments by introducing the “3 Red Lines” rule, the cap on ratio of outstanding property loans to total loans for banks, centralizing the collection of land sales revenue, etc.

Following a number of credit events in 1H2021, the risk aversion stance will probably prevail in the offshore bond market and investors may favor IG issuers and issuers with strong financial positions. Therefore, we expect the credit polarization to continue and intensify going into 2H2021. IG Issuers with strong financial positions will maintain their access to funding channels. They will also likely enjoy lower financing costs. On the contrary, issuers with weak financial positions will face difficulty in raising funds. Some of these issuers may have to go through a number of alternatives for their financing needs, such as asset disposals or debt restructuring consolidation.

Inflation Expectation and Currency Risk among Major Macro Risks

On the macro front, the rising inflation expectation and the currency risk of potential RMB depreciation against USD will be the major risks going to 2H2021. US recorded strong GDP growth of 6.4% for 1Q2021, and its inflation rate rose to 5.4% in June. It was mainly driven by the recovery of its consumption and labor market. Together with the concern on the potential exit from the quantitative easing policies, US 10-year treasury yield rose to the peak of 1.7% in March and stayed at the range of 1.4-1.5% at end-1H2021, compared with 0.9% at end-2020. Also, the US Dollar Index rose from c. 90 at end-2020 to c. 92.5 at end-1H2021. On the other hand, China’s inflation rate is also in the uptrend of 1.1% in June.

Generally, the rising inflation expectation in both China and US will hurt investors’ return and raise issuers’ financing costs on new issuance. Also, first-time issuers, in particular Chinese property developers, are more eager to issue offshore USD bond amidst RMB appreciation against USD. It will help to lower their financing costs and increase their net assets in RMB terms. Fluctuation or potential depreciation of RMB may dampen first-time issuers’ willingness to issue offshore USD bonds.

Appendix

List of Lianhe Global's Rated Chinese Property Developers

Issuer Name	Long-term Issuer Credit Rating	Outlook
Yuzhou Group Holdings Company Limited	BB-	Stable
CIFI Holdings (Group) Co. Ltd.	BBB-	Stable
Logan Group Company Limited	BBB-	Stable
Jingrui Holdings Limited	B+	Stable
Redsun Properties Group Limited	BB	Stable
Yango Group Co., Ltd.	BB	Stable
Radiance Holdings (Group) Company Limited	BB	Stable
China Aoyuan Group Limited	BB+	Stable
Golden Wheel Tiandi Holdings Company Limited	B	Stable
LVGEM (China) Real Estate Investment Company Limited	BB-	Stable
Zhongliang Holdings Group Company Limited	BB	Stable
Yincheng International Holding Co., Ltd.	B+	Stable
Sinic Holdings (Group) Company Limited	BB-	Positive
Dexin China Holdings Company Limited	BB-	Stable
Redco Properties Group Limited	BB-	Stable
Shinsun Holdings (Group) Co., Ltd.	BB-	Stable
Jinke Property Group Co., Ltd.	BB+	Stable
Agile Group Holdings Limited	BBB-	Stable
Huijing Holdings Company Limited	B+	Positive
Jiangsu Zhongnan Construction Group Co., Ltd.	BB	Stable
Source: Lianhe Global		

List of Lianhe Global's Rated Corporations and Non-Banking Financial Institution (NBFI)

Issuer Name	Long-term Issuer Credit Rating	Outlook
China Hongqiao Group Limited	BB+	Stable
E-House (China) Enterprise Holdings Limited	BB+	Negative
Fujian Yango Group Co., Ltd.	BB-	Stable
Jiangsu Shagang Group	BBB+	Stable
Lionbridge Capital Co., Ltd.	BB	Stable
Pujiang International Group Limited	BB-	Stable
Source: Lianhe Global		

List of Lianhe Global's Rated LGFVs

Issuer Name	Province/City	Issuer Rating / Outlook

Liangshan Development (Holdings) Group Co., Ltd	Liangshan	BBB-/Stable
Qingdao City Construction Investment (Group) Limited	Qingdao	A-/Positive
Wuxi Construction and Development Investment Corporation Limited	Wuxi	A/Stable
Yancheng Oriental Investment & Development Group Co., Ltd.	Yancheng	BB+/Stable
Zhengzhou Urban Construction Investment Group Co., Ltd.	Zhengzhou	A-/Stable
Source: Lianhe Global		

List of Lianhe Global's Issuance Rating Actions Year-to-date in 2021

Issuer/Obligor Name	Date	Issuance / Long-term Issuance Credit Rating
Dexin China Holdings Company Limited	2021-01-04	BB-
Zhongliang Holdings Group Company Limited	2021-01-05	BB
CIFI Holdings (Group) Co. Ltd	2021-01-05	BBB-
Redsun Properties Group Limited	2021-01-06	BB-
Logan Group Company Limited	2021-01-06	BBB-
Dexin China Holdings Company Limited	2021-01-06	BB-
Golden Wheel Tiandi Holdings Company Limited	2021-01-06	B+
Sinic Holdings (Group) Company Limited	2021-01-18	BB-
Fujian Yango Group Co., Ltd.	2021-03-08	BB-
Jingrui Holdings Limited	2021-03-16	B+
Logan Group Company Limited	2021-03-31	BBB-
Redco Properties Group Limited	2021-04-07	BB-
Jingrui Holdings Limited	2021-04-21	B+
Yango Group Co., Ltd.	2021-04-26	BB
Redco Properties Group Limited	2021-05-07	BB-
CIFI Holdings (Group) Co. Ltd.	2021-05-10	BBB-
CIFI Holdings (Group) Co. Ltd.	2021-05-10	BBB-
Jingrui Holdings Limited	2021-05-12	B+
Redsun Properties Group Limited	2021-05-17	BB
Jinke Property Group Co., Ltd.	2021-05-20	BB+
Jiangsu Shagang Group Company Limited	2021-05-21	BBB+
China Hongqiao Group Limited	2021-06-01	BB+
E-house (China) Enterprise Holdings Limited	2021-06-02	BB+
Shinsun Holdings (Group) Co., Ltd.	2021-06-03	BB-
China Aoyuan Group Limited	2021-06-15	BB+
Redco Properties Group Limited	2021-06-28	BB-
Agile Group Holdings Limited	2021-07-15	BBB-
Huijing Holdings Company Limited	2021-07-19	B+
Source: Lianhe Global		

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