China Offshore Bond Market 2024 Mid-Year Update: Apparent Recovery Underpinned by Strong Refinancing Need

Summary

The China offshore USD bond new issuance climbed to USD38.5 billion in 1H2024, representing a year-on-year ("y-o-y") growth of 51.1% compared with the first half of 2023 ("1H2023"), which was mainly boosted by more favorable financing conditions, strong refinancing needs of some existing issuers and debts restructuring of some defaulted issuers. On the other hand, the new issuance amount of China offshore RMB bonds in 1H2024 (USD16.73 billion) was almost the same as 1H2023, decreasing marginally by 0.1% y-o-y.

The new issuance amount of China local investment and development company ("LIDC") offshore bonds surged to USD20.8 billion in 1H2024, which was nearly doubled compared with 1H2023. Though the government and regulatory authorities carried out more policies to control large and rising outstanding debts, the strong refinancing needs to roll over the offshore debts significantly contributed to the increase of LIDC offshore bond new issuance.

The continuous downturn in the China property market lowered the property buyers' confidence, and the credit defaults of Chinese property developers further curbed the issuance of China real estate offshore bonds. The new issuance amount slumped to USD4.0 billion in 1H2024, downed by 38.1% y-o-y and hit a record low.

Looking forward, since the refinancing demand of LIDCs remained strong and the regulatory authorities recently encouraged entities with decent credit profiles to issue mid- and long-term offshore bonds, we expect the China offshore bond new issuance will continue to grow in 2H2024.

A) China Offshore Bond Market: Review in 1H2024

USD Bond New Issuance Amount Recovered Markedly, While RMB Bond Issuance Decreased Slightly

The China offshore USD bond new issuance soared to USD38.5 billion in 1H2024, representing an increase of 51.1%, compared with the same period in 2023 (USD25.5 billion) (EXHIBIT 1). As the US inflation seemed to be stronger than expectation and the Federal Reserve ("the Fed") hinted at a longer period of tight monetary policy stance, the base rate showed an upward trend in early 2024. Later, since the inflation rate retreated and the labor market slowed down, the expectation of rate cut strengthened and thus drove down the base rate, which was favorable to the financing environment for offshore USD bonds. In addition, as a huge amount of LIDC offshore USD bonds was due in 1H2024, the need to roll over debts stimulated a large number of entities to refinance through issuing offshore bonds, which also contributed to the increase of new issuance. Moreover, the massive debt restructuring (around USD3.7 billion) of some defaulted property issuers also boosted the offshore USD bond issuance.

As for the China offshore RMB bonds, the tightened regulation on Free Trade Zone ("FTZ") bonds brought out in mid-2023 halted the issuance since the second half of 2023. As a result, the China offshore RMB bonds issued in 1H2024 were all dim sum bonds. The China offshore RMB bond new issuance in 1H2024 decreased slightly by 0.1% y-o-y to USD16.7 billion, as the Chinese government and regulatory authorities posed more restrictions on LIDCs' financing activities.

On the other hand, the total amount of China offshore bond defaults showed a downward trend, which fell sharply to USD9.7 billion in 1H2024 from USD33.7 billion in 2023. Most of the default bonds were issued by the property developers and around 91.1% of the total defaults were denominated in USD (EXHIBIT 2).

Short Tenor Still Dominated, Upcoming Maturity Peak in 2025-2026

As the majority of the new bonds were issued for refinancing needs, the short tenor issuance (1-5 years) still dominated with its proportion to the total new issuance increasing to 78.0% in 1H2024 (EXHIBIT 3). The short-term bonds with a maturity of less than 1 year accounted for 7.1% of the total offshore bond new issuance in 1H2024. Bonds with a maturity of 1-3 years constituted more than half of total new issuance for the same period, and the proportion of bonds with a maturity of 3-5 years was 17.8%.

At end-June 2024, the outstanding amount of offshore bonds reached USD678.5 billion (EXHIBIT 4), of which around 56.6% (around USD384.1 billion) will mature between July 2024 and 2026. Specifically, about USD70.4 billion of offshore USD bonds will mature in 2H2024, which was equivalent to 182.7% of the new issuance amount in 1H2024, with the peak of debt repayment in the last quarter of 2024. Furthermore, there will be USD176.9 billion and USD136.9 billion of offshore bonds due in 2025 and 2026, respectively.

Exhibit 1: Total Amount of China Offshore Bond New Issuance

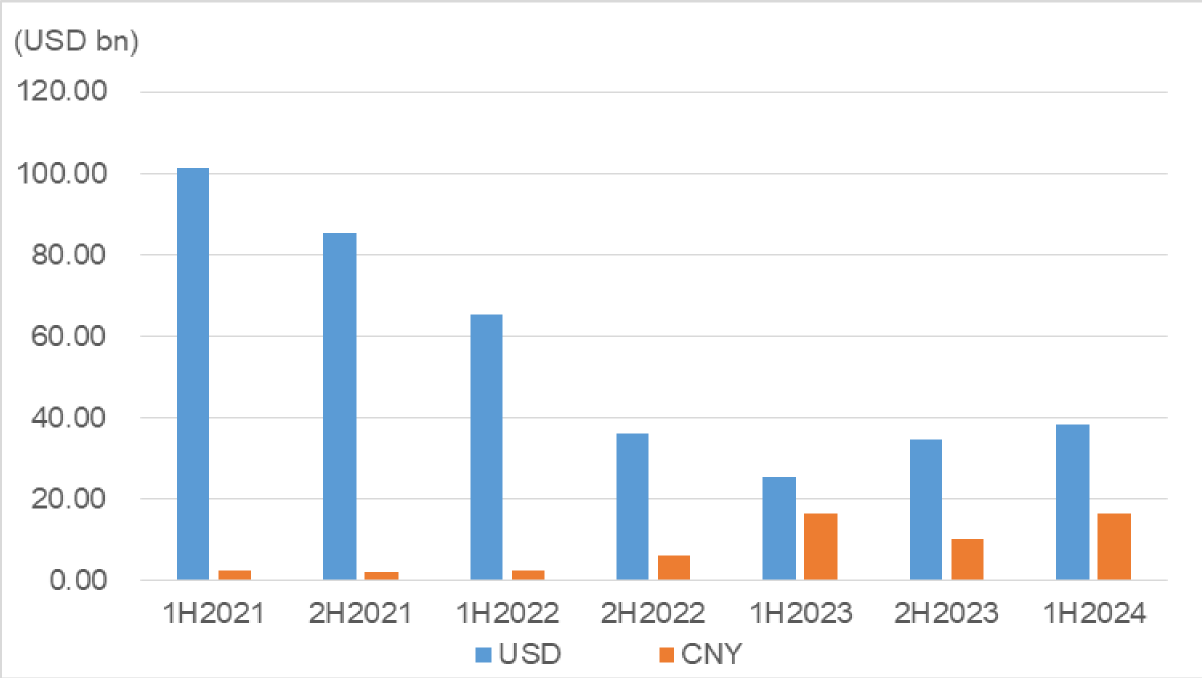


Exhibit 2: Total Amount of China Offshore Bond Defaults

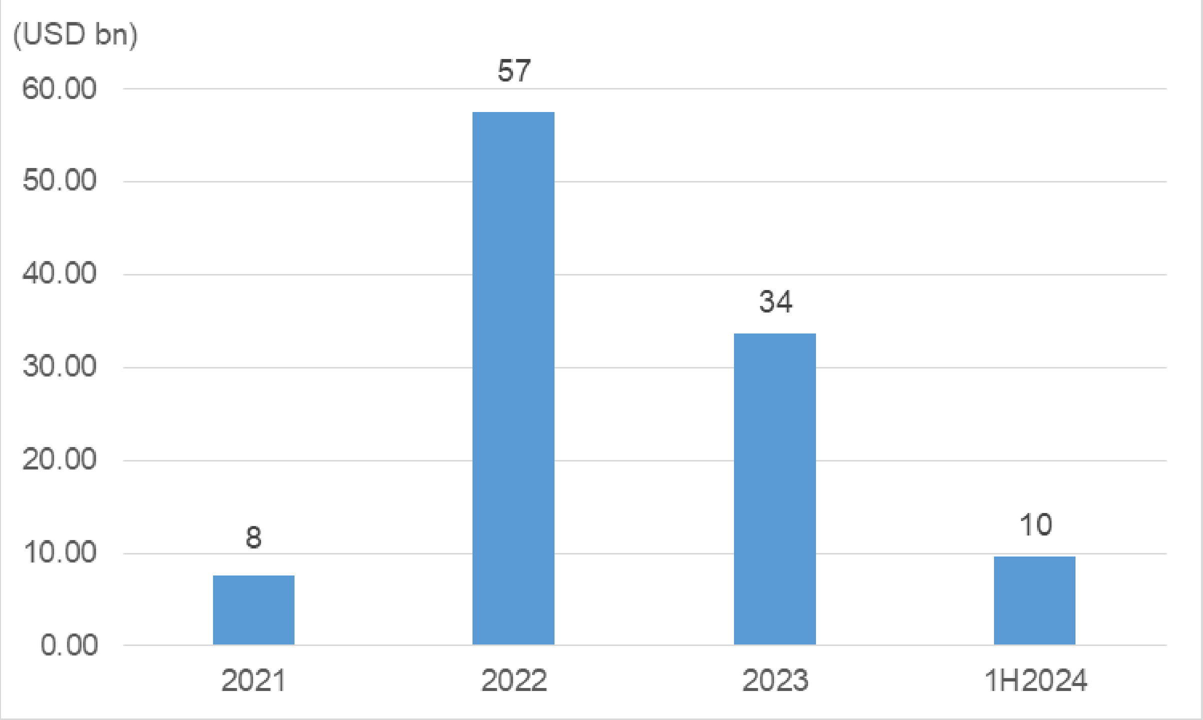


Exhibit 3: Tenor Distribution of China Offshore Bond New Issuance in 1H2024

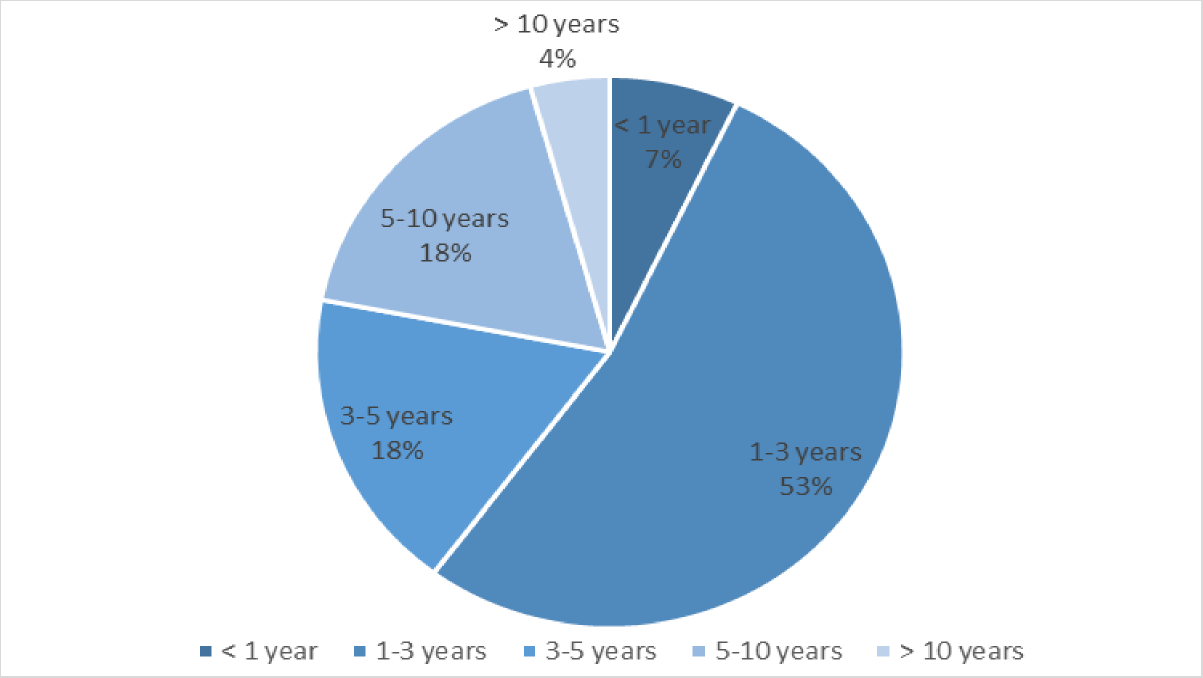
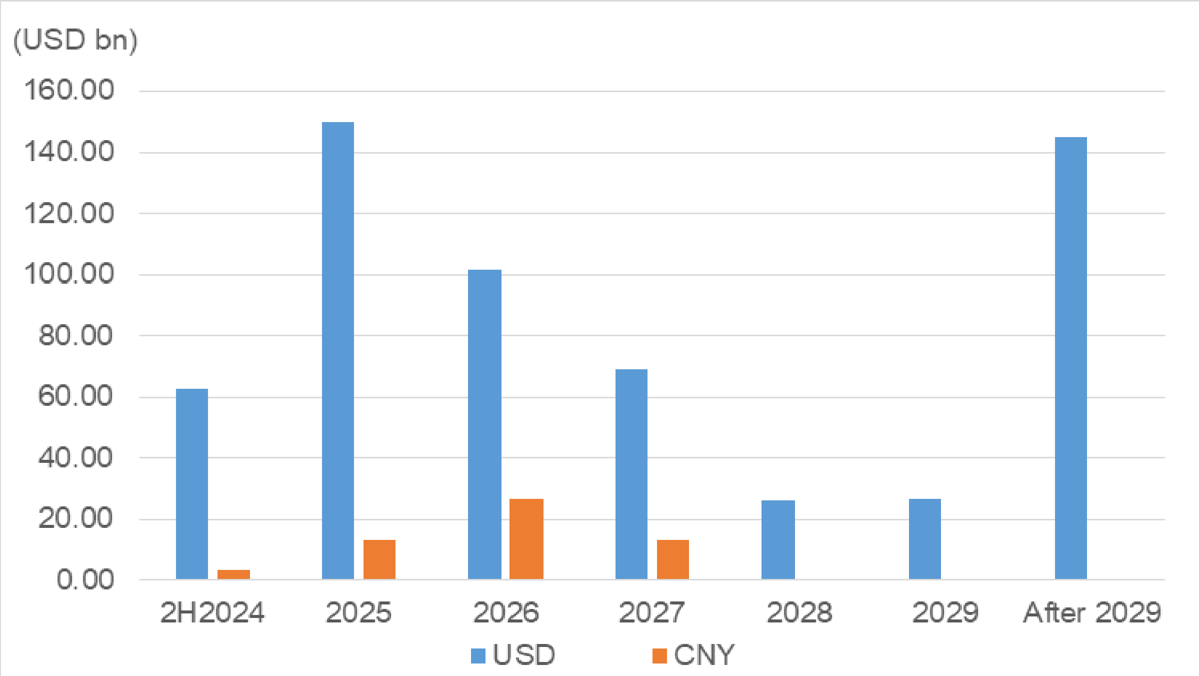


Exhibit 4: Maturity Profile of China Offshore Bond at end-June 2024



B) LIDC: Review of Offshore Bond Issuance in 1H2024

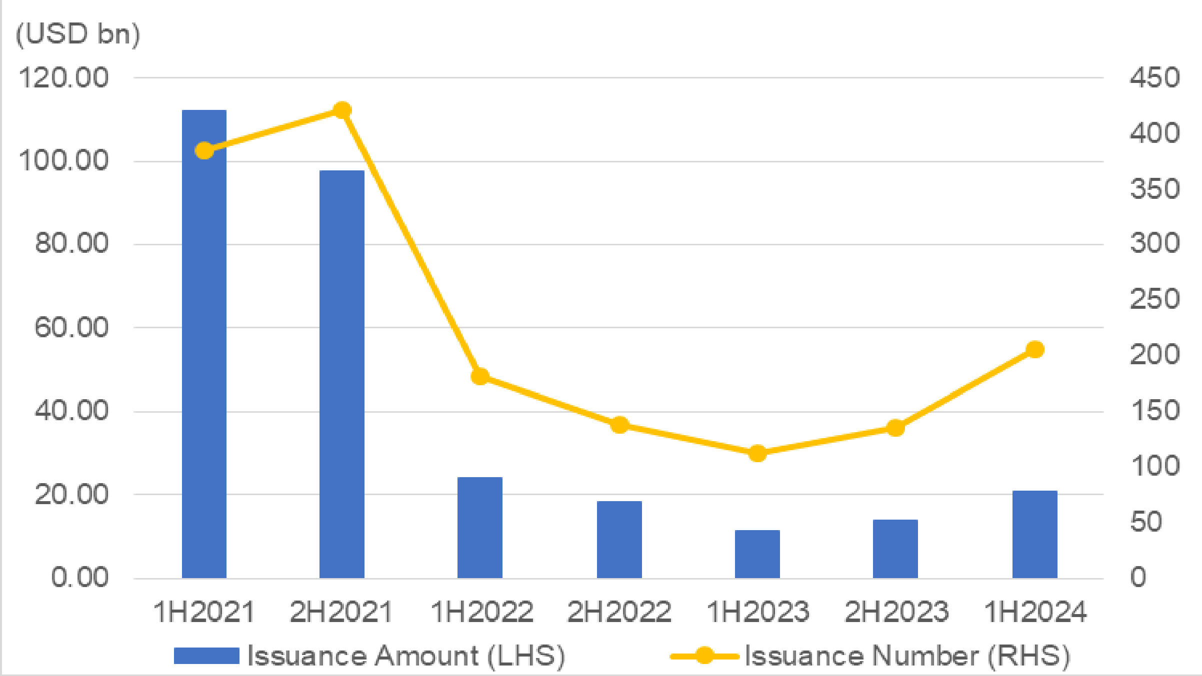
Supported By Strong Refinancing Needs, New Issuance Surged in 1H2024 amid Restrictive Regulations

The issuance of China LIDC offshore USD bonds rebounded to USD20.8 billion in 1H2024 (EXHIBIT 5) from USD11.5 billion in 1H2023, representing a y-o-y growth rate of 81.2%. The central government still posed tight regulations on new offshore debt raising by LIDCs, and the financing costs of offshore USD-denominated bonds were still much higher compared with RMB-denominated bonds. Having said that, LIDCs sped up their refinancing activities through the offshore USD bond issuance as more debts were due in the second quarter of 2024. The new issuance of LIDC offshore bonds were mainly consisted of dim sum bonds in the first few months of 2024.

There were around USD9.8 billion of LIDC offshore bonds matured in 1H2024. LIDC issuers were eager to raise funds and roll over their debts even with higher financing costs, as some of them were not able to repay the large amount of principles, especially for those with weaker credit profiles. To serve their debts more easily, many LIDCs turned to issuing 364-day offshore notes instead of bonds with maturities of more than one year. However, the issuance of 364-day offshore notes was soon suspended under the regulatory guidance in March 2024.

On the other hand, in order to act in concert with the debt disposal policies published by the central government in mid-2023, many provincial governments issued huge amounts of special refinancing debts to replace the outstanding short-term debts of local LIDCs to mitigate their debt burden and enhance market confidence. However, the effectiveness of alleviating liquidity concern on LIDCs by offshore bond issuance was limited, compared with onshore bond issuance. Moreover, the proceed from new issuance by some provinces with severe debt burdens could only be used for refinancing under the central government's requirements, which fueled worries about some LIDCs' capacity to fulfil their responsibilities.

Exhibit 5: Offshore LIDC Bond New Issuance Amount and Number of Issuances



C) Real Estate: Review of Offshore Bond Issuance in 1H2024

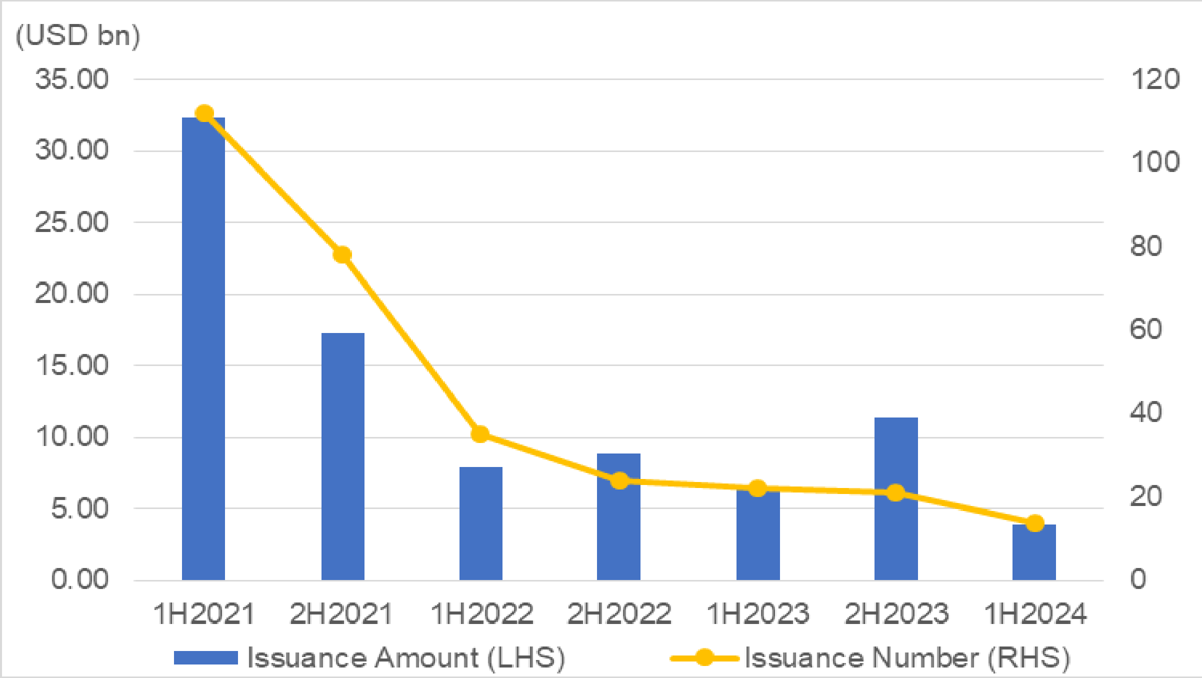
Continued Credit Events Restrained Market Confidence, Majority of New Issuance Derived from Debt Restructuring during Defaults

The new issuance of real estate offshore bonds was cut by almost half in 1H2024, with a total of USD4.0 billion only (EXHIBIT 6). 94.4% of the total new issuance was derived from debt restructuring in the course of defaults. Particularly, there was no issuance in April and May, while the monthly new issuance amounts were all below USD1 billion in January, February and June. There were only 14 new issuances in 1H2024, compared with 22 new issuances in 1H2023. Moreover, the proportion of real estate offshore bonds to the total new offshore issuance downed to below 7% in 1H2024, compared with 14.4% in 1H2023.

In 1H2024, both the central government and local governments set out many policies to relax property purchase requirements and repurchase land from developers under financial pressure to facilitate the development of the real estate market, aid property developers with tight financial conditions and rebuild property buyers' confidence.

However, there were still some credit defaults by Chinese property developers in the offshore bond market. Also, both the demand and supply of real estate offshore bonds remained sluggish. Additionally, the weak property price and contracted sales further restrained property buyers' confidence. Potential homebuyers postponed their purchases over concerns about on-time delivery of new buildings. The credit profile of property developers showed little sign of recovery and those with weaker credit profiles and insufficient cash flows were still vulnerable to liquidity crunch.

Exhibit 6: Offshore Real Estate Bond New Issuance Amount and Number of Issuances



D) China Offshore Bond Market: Outlook in 2H2024

Refinancing Need Continues to Support LIDCs' Issuance

We anticipate that the refinancing need will continue to support the LIDCs' offshore bond issuance in 2H2024. The amount of LIDC offshore bonds maturing in 2H2024 reaches c. USD18.5 billion, while that of maturing in 2025 is in a higher amount of c. USD37.9 billion. The forthcoming debt repayment peak requires a large amount of funds for LIDCs to fulfil their obligations of repayment.

Additionally, recent policies demonstrate some extent of relaxation stance from the central government, as financial institutions and provincial governments are required to support LIDCs' onshore and offshore debt repayments maturing before mid-2027. As a whole, we expect there will be increasing new issuance in the LIDC offshore bond market under the strong refinancing need.

More Supportive Policies in 2H2024

Recently, the People's Bank of China ("PBOC") announced the second interest rate cut in 2024. Besides, the National Development and Reform Commission ("NDRC") published an announcement in late July to encourage entities with decent credit profiles to issue mid- and long-term offshore bonds for high-quality operation, which sent a positive stance on offshore bond issuance. As a whole, we anticipate the offshore bond issuance will continue its recovery trend in 2H2024. The total issuance amount in 2024 is likely to exceed that in 2023.

Analysts

Toni Ho, CFA, FRM
Senior Director
(852) 3462 9578
toni.ho@lhratingsglobal.com

Joyce Huang, CFA
Managing Director
(852) 3462 9586
joyce.huang@lhratingsglobal.com

Media Contact
Alice Wang
(852) 3462 9568
alice.wang@lhratingsglobal.com

Disclaimer

Credit rating and research reports published by Lianhe Ratings Global Limited ("Lianhe Global" or "the Company" or "us") are subject to certain terms and conditions. Please read these terms and conditions at the Company's website: www.lhratingsglobal.com

A credit rating is an opinion which addresses the creditworthiness of an entity or security. Credit ratings are not a recommendation to buy, sell, or hold any security. Credit ratings do not address market price, marketability, and/or suitability of any security nor its tax implications or consequences. Credit ratings may be subject to upgrades or downgrades or withdrawal at any time for any reason at the sole discretion of Lianhe Global.

All credit ratings are the products of a collective effort by accredited analysts through rigorous rating processes. No individual is solely responsible for a credit rating. All credit ratings are derived by a credit committee vesting process. The individuals identified in the reports are solely for contact purpose only.

Lianhe Global conducts its credit rating services based on third-party information which we reasonably believe to be true. Lianhe Global relies on information including, but not limited to, audited financial statements, interviews, management discussion and analysis, relevant third-party reports, and publicly available data sources to conduct our analysis. Lianhe Global has not conducted any audit, investigation, verification or due diligence. Lianhe Global does not guarantee the accuracy, correctness, timeliness, and/or completeness of the information. Credit ratings may contain forward-looking opinions of Lianhe Global which may include forecasts about future events which by definition are subject to change and cannot be considered as facts.

Under no circumstances shall Lianhe Global, its directors, shareholders, employees, officers and/or representatives or any member of the group of which Lianhe Global forms part be held liable to any party for any damage, loss, liability, cost, expense or fees in connection with any use of the information published by the Company.

Lianhe Global receives compensation from issuers, underwriters, obligors, or investors for conducting credit rating services. None of the aforementioned entities nor its related parties participate in the credit rating process aside from providing information requested by Lianhe Global.

Credit ratings included in any rating report are solicited and disclosed to the rated entity (and its agents) prior to publishing. Credit rating and research reports published by Lianhe Global are not intended for distribution to, or use by, any person in any jurisdiction where such use would infringe local laws and regulations. Any user relying on information available through credit rating and research reports is responsible for consulting the relevant agencies or professionals accordingly to comply with the applicable local laws and regulations.

All published credit rating and research reports are the intellectual property of Lianhe Global. Any reproduction, redistribution, or modification, in whole or part, in any form by any means is prohibited unless such user has obtained prior written consent from us.

Lianhe Global is a subsidiary of China Lianhe Credit Rating Co., Ltd. The credit committee of Lianhe Global has the ultimate power of interpretation of any methodology or process used in the Company's independent credit ratings and research.