Issuer Profiles:

EVERRE: Unrated
TIANHL: Unrated

Ticker:

EVERRE
TIANHL

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China Evergrande Group ("EVERRE")

Our take on the situation:

- **On 14 September 2021, the company had announced that due to challenges and uncertainties in improving its liquidity situation, there is no guarantee that the company and its subsidiaries (the "Group") will be able to meet its financial obligations, and if these are not met when due and extensions are not granted, cross-default may be triggered.**
- **Joint financial advisers have been hired to assess its capital structure and liquidity, with a group of USD bondholders also reportedly hiring their own set of advisers.**
- **As implied by bond prices over the past three weeks, the market looks to have reached a consensus over possible debt restructuring in some form for the EVERRE curve.**
- **We see at least six potential confounding factors in a possible debt restructuring including: (1) Large amount of unearned revenue where cash has been received but properties have yet to be completed (2) Guarantees provided on mortgages where buyers may walk-away if properties are unbuilt (3) Lack of information over quantum and specific nature of wealth management products ("WMP") which may be off-balance sheet (4) Large amount of trade and other payables where suppliers themselves may be borrowers and investors in WMP and (5) Lack of details over terms which allowed EVERRE to waive an original redemption (or transfer of further shares in Hengda without consideration) and (6) Other possible off-balance sheet items.**
- **There has been a spillover to the broader Asiadollar high yield market, particularly among China property high yield names lower on the credit scale. Since 1 June 2021, a well followed Asiadollar high yield index has widened significantly though the investment grade index has been fairly stable thus far.**
- **We do not think that other China high yield property names are out of the woods, with heightened possibility of further credit stress across the sector.**
- **In August 2020, regulators announced a proposed new policy popularly named as the "three red-lines" policy that aims to limit additional debt among property developers where reportedly 12 developers were then identified for a pilot study for the policy before full implementation.**
- **While the property development sector is an important contributor to China's economy, concerns over the debt taken by developers have been mounting in recent years, amidst an overriding policy direction that housing is meant to be for living, not for speculation.**
- **Outside of the Asiadollar market, we think the biggest impact will be within the domestic market via EVERRE's linkages to banks and other financial institutions through borrowings, bonds, WMP, mortgages and indirectly through suppliers who may themselves be borrowers within the financial system. While numerous and unwieldy, as a property developer, these interconnections are likely mappable while this is a matter that the People's Bank of China is aware of.**

OCBC Credit Research currently does not cover EVERRE and TIANHL and has not covered EVERRE and TIANHL historically. We have presented this paper as a special interest commentary on the back of investor interest.

Figure 1: EVERRE USD-denominated issues

Bond	Maturity date	Bid Price
EVERRE 8.25% '22s	23/03/2022	26.0
EVERRE 9.5% '22s	11/04/2022	26.0
EVERRE 11.5% '23s	22/01/2023	25.5
EVERRE 10.0% '23s	11/04/2023	25.0
EVERRE 7.5% '23s	28/06/2023	25.0
EVERRE 12.0% '24s	22/01/2024	25.0
EVERRE 9.5% '24s	29/03/2024	25.0
EVERRE 10.5% '24s	11/04/2024	25.0
EVERRE 8.75% '25s	28/06/2025	25.0

Indicative prices as at 20 September 2021 Source: Bloomberg

Figure 2: TIANHL USD-denominated issues

Bond	Maturity date	Bid Price
TIANHL 11.5% '22s	24/10/2022	16.0
TIANHL 13.0% '22s	06/11/2022	16.0
TIANHL 12.0% '23s	24/10/2023	15.0
TIANHL 13.75% '23s	06/11/2023	15.0

Indicative prices as at 20 September 2021 Source: Bloomberg

Background

- China Evergrande Group ("EVERRE"), incorporated in the Cayman Islands, is listed on the Hong Kong Stock Exchange. Headquartered in Shenzhen, the company and its subsidiaries (the "Group") focuses on property development across China.
- The company's market cap was HKD30.2bn (~USD3.9bn) as at 20 September 2021, having fallen from HKD187.2bn (~USD24.1bn) at the beginning of the year. The company's shareholding is highly concentrated, with the company's founder/Chairman holding a ~77%-stake.
- By property sales, EVERRE is among China's largest property company, where the China property market is highly fragmented. In 2020, the company's total contracted sales was RMB723.3bn (~USD111.9bn). The provinces of Guangdong, Jiangsu and Zhejiang contributed ~27% to this total. Projects in other provinces contributed less than 6% each to total contracted sales.
- The company is a bellwether issuer in the China high yield property bond market. Per Bloomberg data, there are USD14bn of bonds outstanding that have been issued by EVERRE (the listed entity) and another ~USD5.2bn issued by Scenery Journey Ltd ("TIANHL", incorporated in the British Virgin Islands, is an indirect wholly-owned subsidiary of EVERRE). EVERRE also has onshore bonds issued by Hengda Real Estate Group Company Limited ("Hengda", 59.9%-owned by EVERRE as at 31 December 2020).
- Concurrent with the release of its unaudited 1H2021 results announcement in August 2021, it was announced that Group has risks of defaults on borrowings and cases of litigation outside its normal course of business.
- Prior to events in recent weeks which points towards significant liquidity stress at the company and a possible debt restructuring, there had been questions over EVERRE's liquidity situation, most recently in September 2020.
- In August 2020, regulators announced a proposed new policy popularly named as the "three red-lines" policy that aims to limit additional debt among property developers where reportedly 12 developers were then identified for a pilot study for the policy before full implementation.
- While the property development sector is an important contributor to China's economy, concerns over the debt taken by developers have been mounting in recent years, amidst an overriding policy direction that housing is meant to be for living, not for speculation.

What is happening at EVERRE?

On 14 September 2021, the company had announced that due to challenges and uncertainties in improving its liquidity situation (asset disposals and expected decline in new property sales), there is no guarantee that the Group will be able to meet its financial obligations. If these obligations are not met when due and extensions are not granted, cross-default may be triggered. The company also disclosed that two subsidiaries failed to discharge guarantee obligations on wealth management products ("WMP") issued by third parties amounting to RMB934mn (~USD144.5mn). WMP are typically bought by retail investors and reportedly buyers include the company's employees and suppliers.

The company also announced that it has hired joint financial advisers to assess the capital structure of EVERRE and its subsidiaries (collectively, the "Group's")). They will also evaluate the liquidity and explore all feasible solutions to ease the current liquidity issue and reach an optimal solution for all stakeholders as soon as possible. Last week, a group of USD bondholders was reported by the media to have appointed financial and legal advisers to represent their interest.

Figure 3: Timeline of key events since 19 August 2021

Date	Brief Description
19 August 2021	• Executives reportedly summoned to a meeting with representatives from the People's Bank of China ("PBOC") and the China Banking and Insurance Regulatory Commission where the company was asked to resolve its debt issues without destabilising property and capital markets. • The founder had also reportedly stepped down from chairmanship at Hengda in the same week.
25 August 2021	• Company announces profit warning as it expects a y/y decline in net profit for 1H2021.
31 August 2021	• Announced unaudited interim financial results for 1H2021. • Stated that the Group has risks of defaults on borrowings and cases of litigation outside its normal course of business.
2 September 2021	• Reportedly at least two non-bank creditors have accelerated payment on certain loans.
14 September 2021	• Company announces the appointment of joint financial advisers to assess its capital structure and resolve its liquidity issues. • Announced that there is no guarantee that the Group will be able to meet its financial obligations under the relevant financing documents and if these are not met when due and extensions are not granted, cross-default may be triggered. • Reportedly Guangdong province officials had appointed advisers to assess EVERRE.
15 September 2021	• Reportedly the Ministry of Housing and Urban-Rural Development has told major banks that the company will not be able to make loan interest payments due 20 September 2020.

Source: Company, Bloomberg, Reuters
Note: This list is non-exhaustive

The Group faces interest payments on its bonds this week including:

Figure 4: Interest payments on bonds

Issue	Amount Outstanding (USDmn)	Date	Coupon Payment (USDmn)
EVERRE 8.25% '22s	2,025	23 September 2021	83.5
EVERCN 5.8% '25s	~619	23 September 2021	~36
EVERRE 9.5% '24s	951	29 September 2021	45.2
Total			164.7

Source: OCBC Credit Research tabulated from Bloomberg data
Note: The EVERCN 5.8% '25s is an onshore bond issued by Hengda; an earlier version has the coupon payment at ~USD17.9mn, this has been updated

While the company's consolidated unadjusted gross debt-to-equity ratio improved from 2.8x in end-2016 to 2.0x in end-2020, with the ratio falling further to 1.4x as at 30 June 2021, it is worth noting that this only accounts for on-balance sheet borrowings while other types of liabilities increased in the meantime. The denominator also includes the existence of a high proportion of minority interest (at 54% of total equity as at 30 June 2021) compared to end-2016 when this was below 20%. Additionally, short term maturities have been a large part of total debt, with the company historically reliant on continuous access to financing markets (including the Asiadollar high yield market) for refinancing.

What is the market saying?

While attention over EVERRE had intensified in recent weeks, EVERRE's liquidity outlook had dampened since early June 2021, with bond prices steadily falling in the past 3.5 months and downgrades by external credit rating agencies (first downgrade during this wave started in June 2021). As of writing, the company's external ratings have been lowered to a level where the external credit rating agencies view a default of some kind as foreseeable.

The EVERRE curve has been trading on recovery values with cash bid prices falling below 30 and staying there for much of the past three weeks, signaling that the market is viewing the company as a default candidate. As of writing, the largest bond outstanding under the EVERRE ticker, namely the ~USD4.68bn EVERRE 8.75% '25s, is trading at the 25/26 bid-ask level. The shortest dated bond, the EVERRE 8.25% '22s maturing in March 2022 is trading at 26/27 bid-ask level. These bonds are issued by the Hong Kong listed entity which owns an office building in Wanchai, Hong Kong (reportedly bought for USD1.6bn in 2015) and a controlling stake in China Evergrande New Energy Vehicle Group. This Hong Kong listed entity is still loss-making.

The TIANHL curve has been trading at lower prices than the EVERRE curve. The TIANHL 11.5% '22s, which has an amount outstanding of USD2.0bn and is the shortest dated TIANHL bond, is trading at the 16/18 bid-ask level. These TIANHL bonds are guaranteed by Tianji Holding Limited ("Tianji", incorporated in Hong Kong, where Tianji is a subsidiary of Hengda) and the keepwell provider is Hengda.

The Group also has onshore bonds (under the "EVERCN" ticker, issued by Hengda) amounting to RMB53.5bn (~USD8.3bn). Reuters reported that Hengda had requested for the bonds to be put on trading halt on 16 September 2021. On 15 September 2015, a domestic rating agency had downgraded the bonds, with the issuer and bonds put on watch for possible further downgrades. The largest bond outstanding under the EVERCN ticker, namely the RMB15bn EVERCN 6.27% '23s had a bid price of 30 on 17 September 2021 per Bloomberg data. Despite Hengda being the Group's main onshore unit, which would indicate that it sits closer to property development assets, its bond prices are not much higher than the offshore EVERRE curve.

Potential confounding factors

We see at least six main confounding factors on any possible debt restructuring:

(1) Contract liabilities of RMB215.8bn (~USD33.4bn) as at 30 June 2021, indicating obligations towards large number of property buyers where cash payments had been received but goods and services have not been delivered. As at 30 June 2021, ~54% of total assets were uncompleted property under development whose asset value would only be optimized if completed. In addition to funding needs for interest servicing and debt repayments, the company is also facing significant funding needs to fulfill its obligations on completing properties which had been sold.

(2) Common across the industry, the Group has provided guarantees in respect of mortgage facilities for certain buyers (end-2020: RMB550.2bn (~USD85.1bn)). As far as we are aware, as property units gets completed on time and handed over to buyers, usually this was not a problem among Asiadollar China high yield property bond issuers while sector-wide mortgage default rates have also been historically low. However, it is conceivable that with heightened risk of delay in completion, some buyers may consider mortgage default to be a real option. Given the large quantum of buyers, uncompleted properties and mortgages, a more coordinated resolution may require other developers to take over property projects.

(3) Lack of information over the exact amount and specific nature of obligation that the company has on the WMP, which may be off-balance sheet. The company appears to be prioritizing paying back investors of these products (largely retail investors), with investors reportedly being offered assets as part of a repayment plan. We found no public mention of the amount of such obligations, though Caixin, a media outlet reported that RMB40bn (~USD6.2bn) of WMP are due.

(4) Large amount of trade and other payables which includes amounts owed to suppliers. As at 30 June 2021, this was RMB951.1bn (~USD147.1bn), making up 48% of total on-balance sheet liabilities. Reportedly, some supplier bills have been unpaid while certain suppliers are also investors in WMP.

(5) As a recap, Hengda has existing minority investors, with EVERRE holding 59.9% of Hengda as at 31 December 2020. As part of a 2017 investment agreement at Hengda, the minority investors may

require EVERRE to repay their investment (or transfer additional shares to them at no consideration) if a public listing of Hengda did not occur by 31 January 2021. With regulatory approval not forthcoming and a prospect of a public listing dimmed, in September 2020, an agreement was reached such that repayments that were due and worth RMB130bn (~USD20.1bn) could be deferred and Hengda remains an unlisted entity. However, little is known what new terms were agreed with these minority investors in lieu of the original arrangement.

(6) Other type of off-balance sheet liabilities which reportedly may include amounts owed on past acquisitions that were unpaid on account of legal technicalities.

Figure 5: Selected income statement items

RMB bn	1H2021	1H2020
Revenue	222.7	266.6
Gross profit	28.8	66.7
Operating profit	25.7	47.4
Net profit	10.5	14.8

Source: Company's financials

Figure 6: Selected on-balance sheet items

RMB bn	30 June 2021	31 December 2020
Short term borrowings	240.0	335.5
Long term borrowings	331.7	381.0
Trade and other payables	951.1	829.2
Contract liabilities	215.8	185.7
Other liabilities	227.9	219.3
Total Liabilities	**1,966.5**	**1,950.7**
Minority interest	220.2	203.5
Equity (excluding minority interest)	190.8	146.9
Properties under development	1,279.0	1,257.9
Completed properties held for sale	144.5	148.5
Investment properties	155.4	165.9
Other assets	798.7	728.9
Total Assets	**2,377.6**	**2,301.2**

Source: Company's financials
Note: (1) Other liabilities consist mainly of current income tax liabilities and deferred tax liabilities
(2) Other assets consist of a variety of assets including trade and other receivables, investments, prepayments and cash

What has happened in the broader market?

Since 1 June 2021, a well-followed Asiadollar high yield index has widened significantly though the investment grade index has been fairly stable thus far. In our view, this is indicative that bond investors were still differentiating between the two markets and largely saw this to be a China high yield property market matter in the past months.

As at 17 September 2021 and reflecting the significant price decline, EVERRE and TIANHL bonds make up 2.0% of a well tracked Asiadollar high yield index which tilts heavy on bonds issued by property issuers. China high yield property bonds lower on the credit rating scale have taken a significant negative impact in September 2021, trading at stressed levels of below 80 and bonds of certain issuers are trading in the 40-70 range. While stronger China property high yield issuers and those in the crossover bucket was relatively unscathed earlier, prices had dropped by a few ppt towards the end of last week. Bonds issued by benchmark investment grade property issuers has dropped slightly, which points towards considered moves rather than indiscriminate selling thus far.

Given the heightened measures imposed to rein in leverage of the sector, it is not far-fetched for investors to focus on those issuers who are highly indebted. These issuers tend to be highly reliant on refinancing, with hampered ability to pay down debt from internal sources and are also at the highest risk to shift debt off-balance sheet. A prolonged increased in cost of funding for the sector (assuming market access is still available) would also negatively drag profitability, thus further

weakening credit fundamentals.
In the primary market, Asiadollar bond issuance since 1 January 2021 to 20 September 2021 was cumulatively USD285.8bn, higher than the USD262.7bn same time last year, driven by an observably quieter primary issuance since June 2021 per Blomberg data. However, investment grade issuers who came to tap the market still managed to see decent demand, particularly issuers outside of China as investors started diversifying their portfolios.

For much of August 2021, China's 5-year credit default swaps was tightening and was very stable until 16 September 2021. As of writing, the CDS has seen a 11bps widening to 46bps from 16 September 2021, marginally above the time where the investment grade market was stressed over China Huarong Asset Management Co Ltd concerns. On 17 September 2021, the PBOC added RMB90bn (~USD14bn) on a net basis through 7-day and 14-day reverse repurchase agreements, which the market is seeing as higher than usual. Prior to 17 September 2021, interbank market liquidity was relatively stable. The USD/CNH foreign exchange rate has depreciated slightly by 0.4% since 16 September 2021.

A handful of China developers had issued SGD-denominated bonds in the past though EVERRE has not been an issuer in this market. As of writing, there are no significant China property bonds outstanding in SGD. We expect negative spillover to SGD, if any, to be driven by investor sentiment and affecting the true high yield space while the rest of the SGD high grade space could benefit from potential flight to safety, in our view.

Conclusion

As implied by bond prices, the market looks to have reached a consensus over possible debt restructuring in some form or other for the EVERRE curve. We do not think that other China high yield property names are out of the woods, with heightened possibility of further credit stress across the sector. Outside of the Asiadollar market, we think the biggest impact will be within the domestic market via EVERRE's linkages to banks and other financial institutions through borrowings, bonds, WMP, mortgages and indirectly through suppliers who may themselves be borrowers within the financial system. For example, EVERRE is a significant shareholder of a regional bank where connected transactions have been reported. On the back of contagion fears, share prices of China property companies, certain banks and insurers have seen their share price fall on the back of contagion fears. In June 2021, the People's Bank of China ("PBOC") was reported to have asked major creditors of EVERRE to conduct stress test on their exposure to the company, indicating this is a matter that the PBOC is aware of. While numerous and unwieldy, as a property developer, these interconnections are likely mappable (including the WMP where investors have been reported to consist of retail investors, employees and suppliers).

Explanation of Issuer Profile Rating / Issuer Profile Score

Positive ("Pos") – The issuer's credit profile is either strong on an absolute basis, or expected to improve to a strong position over the next six months.

Neutral ("N") – The issuer's credit profile is fair on an absolute basis, or expected to improve / deteriorate to a fair level over the next six months.

Negative ("Neg") – The issuer's credit profile is either weaker or highly geared on an absolute basis, or expected to deteriorate to a weak or highly geared position over the next six months.

To better differentiate relative credit quality of the issuers under our coverage, we have further sub-divided our Issuer Profile Ratings into a 7 point Issuer Profile Score scale.

IPR	Positive		Neutral			Negative	
IPS	1	2	3	4	5	6	7

Please note that Bond Recommendations are dependent on a bond's price, underlying risk free rates and an implied credit spread that reflects the strength of the issuer's credit profile. Bond Recommendations may not be relied upon if one or more of these factors change.

Explanation of Bond Recommendation

Overweight ("OW") – The bond represents **better relative value** compared to other bonds from the same issuer, or bonds of other issuers with similar tenor and comparable risk profile.

Neutral ("N") – The represents **fair relative value** compared to other bonds from the same issuer, or bonds of other issuers with similar tenor and comparable risk profile.

Underweight ("UW") – The represents **weaker relative value** compared to other bonds from the same issuer, or bonds of other issuers with similar tenor and comparable risk profile.

Other

Suspension – We may suspend our issuer rating and bond level recommendation on specific issuers from time to time when OCBC is engaged in other business activities with the issuer. Examples of such activities include acting as a joint lead manager or book runner in a new issue or as an agent in a consent solicitation exercise. We will resume our coverage once these activities are completed.

Withdrawal ("WD") – We may withdraw our issuer rating and bond level recommendation on specific issuers from time to time when corporate actions are announced but the outcome of these actions are highly uncertain. We will resume our coverage once there is sufficient clarity in our view on the impact of the proposed action.

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Analyst Declaration

The analyst(s) who wrote this report and/or her or his respective connected persons did not hold financial interests in the following above-mentioned issuers or companie as at the time of the publication of this report.

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