

# Chinese Dollar Bond Market Report

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Date: February 28, 2020

# CXI & CXAP 2019 Chinese Dollar Bond Market Report

## 2019 Chinese Dollar Bond Market Recap

- **Under the circumstances of improved financing environment and strong demand for issuance, the new issuance of Chinese dollar bonds has picked up in 2019.** A total of 608 dollar bonds were issued by Chinese issuers in 2019, with an issuance amount of USD204.8 billion, up 25.9% and 26.4% YoY respectively. On a quarterly basis, the issuance amount in 2019 rose first and then fell.
- **New issuance of Chinese real estate and Chengtou dollar bonds reached a record high.** Real estate companies, financial institutions and Chengtou enterprises are the main issuers of Chinese dollar bonds, accounting for 35.5%, 16.9% and 13.2% of the total issuance amount in 2019, respectively.
- **In 2019, the average coupon rate of newly issued Chinese dollar bonds showed a downward trend, felling from 6.9% in 2019Q1 to 5.3% in 2019Q4. The average tenor of newly issued Chinese dollar bonds in 2019 is longer than that in 2018, increasing from 3.36 years in 2018 to 3.61 years in 2019.**
- **The lack of credit rating phenomenon still existed, 98 issuers did not obtain the public rating from the three international rating agencies, accounting for 30.1% of all issuers. The number of high-yield bond issuers increased significantly, increasing from 62 high-yield bond issuers in 2018 to 110 in 2019.**
- **Driven by the Fed's interest rate cut, the price of Chinese dollar bonds rose sharply in 2019, and real estate bonds performed the best.**

## Rating Actions and Credit Events

- **The proportion of onshore negative rating actions decreased, while that of offshore negative rating actions was relatively high.** In 2019, there were 371 issuer rating adjustment actions in the onshore market, and the number of downgrades was 150 times, accounting for 40.4% of the total rating actions; there were 147 issuer rating adjustment actions in the offshore market, of which 96 were negative rating actions, accounting for 65.3% of the total rating actions, which mainly focused on real estate, Chengtou, industrial and consumer discretionary sectors.
- **Default events occurred frequently in the onshore market, and the default issuers were mainly private enterprises. The risk of individual credit events in the offshore dollar bond market may deserve more attention.**

## Sector Overview and Development Trend

- **In 2019, new issuance of Chinese real estate dollar bonds reached a record high, and the issuance rose first and then fell.** In 2019, 186 Chinese real estate dollar bonds were issued, with an amount of USD72.7 billion. As Chinese real estate dollar bonds were mainly high-yield issues, the average coupon rate increased by 113.6 basis points YoY to 8.90%. **In addition, the credit profile of real estate issuers continued to differentiate.**
- **New issuance of Chengtou dollar bonds continued to grow, and a large number of new issuers emerge.** In 2019, 104 dollar bonds were issued by Chengtou enterprises, with an amount of USD27.0 billion, up 40.5% and 38.6% YoY respectively. The average coupon rate of Chengtou dollar bonds in 2019 was lower than that in 2018. **The penetration of credit rating was weak for Chengtou issuers, high-yield bond issuers were active, and lower-tier issuers has appeared.**

## Outlook

- **In 2020, in view of the refinancing demand of outstanding issuers, it is expected that the market of Chinese dollar bonds would continue to expand. However, given the outbreak of coronavirus, the issuance may fall first and then rise. It is expected that the issuance cost may have downward trend but with limited room, and the average tenor may be extended.**
- **In terms of credit risk, we believe that the credit profile of real estate issuers would continue to diverge, and the credit trend of Chengtou enterprises with weak financial strength and low administrative level would be closely monitored.**

## Introduction

The loosening of global liquidity in 2019, coupled with the continuous recovery of market confidence in Chinese issuers<sup>1</sup> since 2018Q4, has formed a positive effect on the Chinese dollar bond market<sup>2</sup>. At the same time, there was a peak of maturity for the outstanding bonds, with the refinancing demand of outstanding issuers and the emergence of new issuers, promoting the continuous expansion of the Chinese dollar bond market, and the outstanding volume has risen from USD618.2 billion at the end of 2018 to USD729.9 billion at the end of 2019. Given the uncertainties of China-US trade policy, global economic growth has slowed down. In order to support economic development, central banks around the world have cut interest rates. The Federal Reserve has cut interest rates three times since July, resulting in a downward trend in the yields of US Treasury bonds as well as in the issuance cost of dollar bonds. Although credit events have occurred occasionally in the Chinese dollar bond market, they are mostly individual events. In addition, with the market consensus of the accumulation and release of credit risk, the impact of these credit events is limited. Overall, both the primary and secondary markets of Chinese dollar bonds in 2019 outperformed that in 2018.

## 2019 Chinese Dollar Bond Market Recap

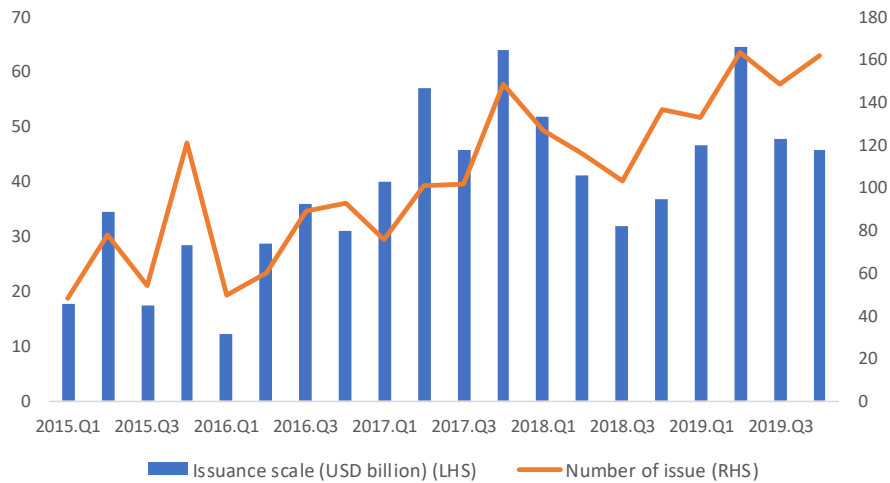
### *Primary Market*

**Under the circumstances of an improved financing environment and a strong demand for issuance, the new issuance of Chinese dollar bonds has picked up in 2019.** A total of 608 dollar bonds were issued by Chinese issuers in 2019, with an issuance amount of USD204.8 billion, up 25.9% and 26.4% year-on-year (YoY) respectively. On a quarterly basis, the issuance amount in 2019 rose first and then fell. In the first half of 2019, the National Development and Reform Commission (NDRC) extended the validity period of some issuers' foreign debt approval documents. Enterprises that failed to complete the issuance of dollar bonds in 2018 did not need to re-register the issuance of foreign debt, which accelerated the issuance speed. Combined with the improvement of liquidity at the beginning of the year, the new issuance of Chinese dollar bonds continued to rise and the total issuance amount in the second quarter (USD64.7 billion) was the highest for a single quarter. However, as the China-U.S. trade war has escalated again in the second half of 2019, leading to a sharp depreciation of RMB, the cost of issuance of dollar bonds has increased relatively. Therefore, compared with the second quarter, the issuance of Chinese dollar bonds in the third and fourth quarter dropped significantly. However, compared with the data of the past five years, the new issuance in the third and fourth quarter of 2019 are at relatively high level, reflecting the strong demand of Chinese issuers for dollar bonds.

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<sup>1</sup> Refers to the credit entity

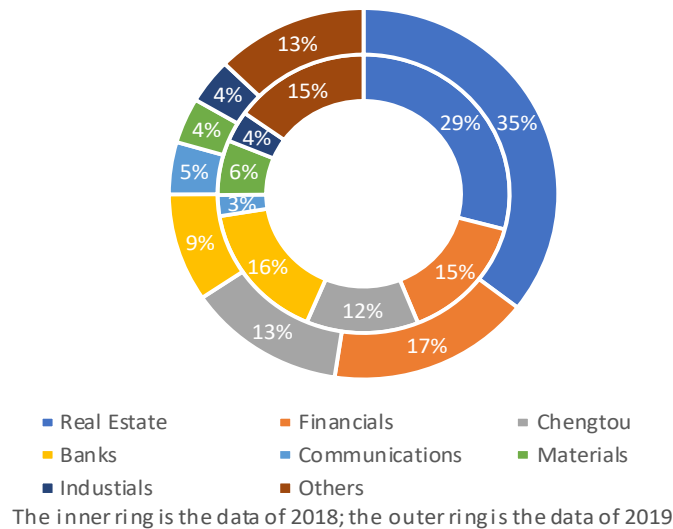
<sup>2</sup> Refers to bonds issued by Chinese enterprises and denominated in US dollars

**Exhibit 1: New issuance of Chinese dollar bonds from 2015 to 2019**

Source: Bloomberg, CCXAP Research

**New issuance of Chinese real estate and Chengtou dollar bonds reached a record high.** Real estate companies, financial institutions and Chengtou enterprises are the main issuers of Chinese dollar bonds, accounting for about 35.5%, 16.9% and 13.2% of the total issuance amount in 2019, respectively. Among them, the issuance amount of real estate and Chengtou enterprises reached a record high of USD72.7 billion and USD27 billion. In addition, due to the downward pressure on the China's economy and the weakening operating environment of financial institutions, Chinese banks slowed down their asset expansion, and the issuance of dollar bonds by Chinese banks has declined significantly for two consecutive years. In terms of issuance amount, it decreased from USD45.1 billion in 2017 to USD19.3 billion in 2019, and its proportion decreased from 21.8% to 9.4% respectively.

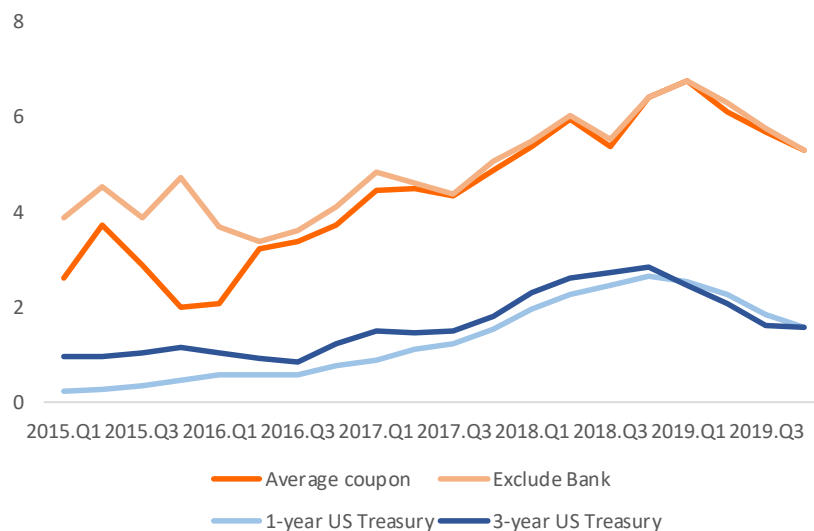
**Exhibit 2: Issuance amount in 2018 and 2019 by sector**



Source: Bloomberg, CCXAP Research

**In 2019, the average coupon rate of newly issued Chinese dollar bonds showed a downward trend.** Affected by the increase of high-yield Chinese real estate dollar bond issuance, the average coupon<sup>3</sup> in the first quarter of 2019 is higher than that in the fourth quarter of 2018. But in the whole year, with the decline of US Treasury bond yields and the slowdown of Chinese real estate dollar bond issuance in the second half, the average coupon of Chinese dollar bond fell from 6.78% in 2019Q1 to 5.32% in 2019Q4.

**Exhibit 3: Average coupon rate and US Treasury yields (%)**

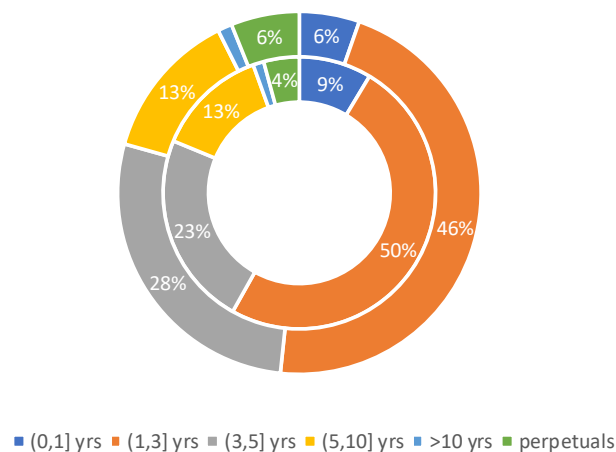


Source: Bloomberg, Fed, CCXAP Research

<sup>3</sup> Only bonds with fixed coupon rate and no call or put provisions were counted

The average tenor of newly issued Chinese dollar bonds in 2019 is longer than that in 2018, increasing from 3.36 years in 2018 to 3.61 years in 2019. The issuance of Chinese dollar bonds with tenor less than one year in 2019 has declined compared with that in 2018. The number of issuances has decreased from 107 in 2018 to 98 in 2019, and the amount of issuance has decreased from USD14.0 billion to USD11.0 billion due to the narrowing of the yield spreads between US medium and short-term Treasury bonds and the recovery of investor confidence, which is conducive to the issuance of long-term dollar bonds. The medium-term dollar bonds (with tenor ranges from one to five years) are still the main issue types, with 430 issues and USD151.5 billion, accounting for about 74.0% of the total issuance.

**Exhibit 4: Issued amount in 2018 and 2019 by tenor**



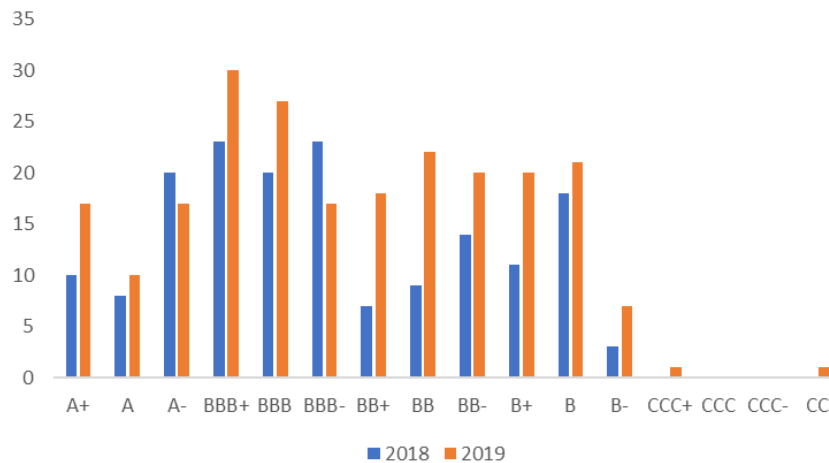
The inner ring is the data of 2018; the outer ring is the data of 2019

Source: Bloomberg, CCXAP Research

**The lack of credit rating phenomenon still existed, and the number of high-yield issuers has increased significantly.** Of the 326 Chinese issuers in 2019, 109 were first-time dollar bonds issuers, among which 49 were Chengtuo enterprises, 22 were financial institutions and 12 were real estate companies. The lack of rating of Chinese dollar bond issuers, especially new issuers, is still serious. Among all the issuers in 2019, 98 did not obtain the public rating from the three international rating agencies, accounting for 30.1% of all issuers; among all the new issuers in 2019, 51 have no public rating, accounting for 46.8% of all new issuers. Among the issuers without public rating, the majority were first-time Chengtuo enterprises and financial institutions dollar bonds issuers, with 25 and 12 issuers respectively, and most of them are controlled by local governments. Among the issuers with

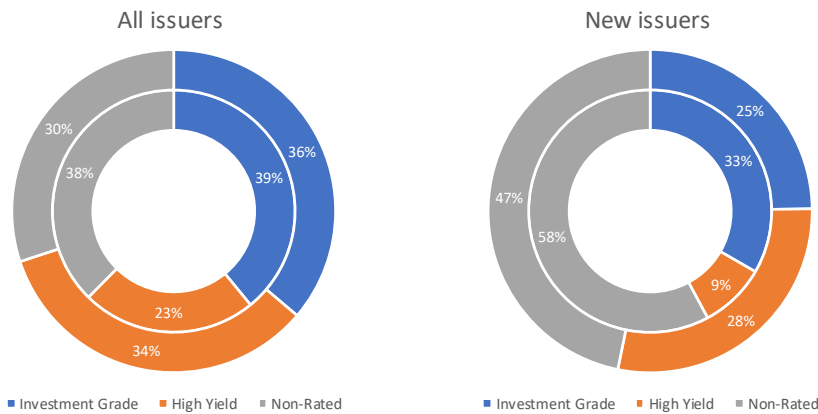
public rating<sup>4</sup>, the number of high-yield bond issuers increased significantly from 62 in 2018 to 110 in 2019. This is mainly because the rising credit risk in 2018 had weakened investors' confidence in high-yield bonds, and the issuance of high-yield dollar bonds improved with the gradual recovery of investors' confidence in 2019.

**Exhibit 5: Issuer rating distribution in 2018 and 2019**



Source: Bloomberg, CCXAP Research

**Exhibit 6: Issuer credit rating distribution in 2018 and 2019**



Source: Bloomberg, CCXAP Research

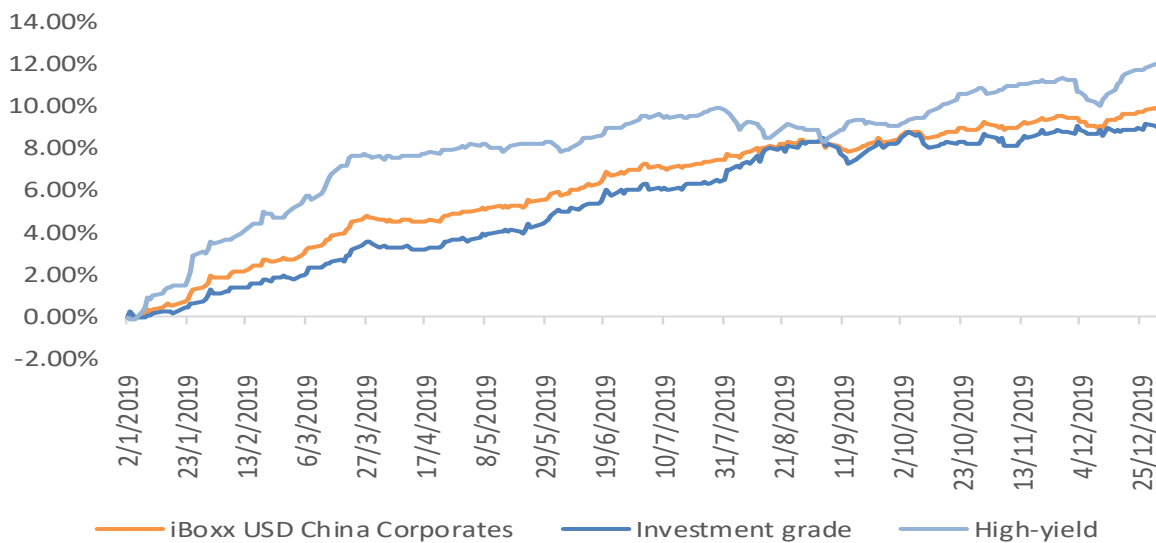
**Secondary market**

**Driven by the Fed's interest rate cut, the price of Chinese dollar bonds rose sharply in 2019.** At the beginning of 2019, the Federal Reserve changed from hawkish to dovish and cut interest rates three times, together with the market's pessimistic expectation of the US economic growth prospects, driving the US Treasury bond yields down in 2019. In addition,

<sup>4</sup> Data as of end-2019. If there are differences in the credit rating of the three international rating agencies, the statistics shall be based on the highest rating

the investors' risk preference rebounded, attracting foreign capital to the higher-premium dollar bond market and driving its price up. By the end of 2019, the one-year return of iBoxx China dollar bond index was 9.88%, that of investment grade bonds index was 9.01%, and that of high-yield bonds index was 12.06%. In terms of credit spreads, due to the improvement of domestic financing environment in the first half of the year and the easing of trade friction between China and US in the second half of the year, market sentiment improved, and the average spreads of Asian investment grade and high-yield dollar bonds narrowed 47.3bps and 136.9bps respectively.

**Exhibit 7: Returns of Chinese dollar bonds in 2019<sup>5</sup>**



Source: Bloomberg, CCXAP Research

**Market risk appetite has picked up and real estate bonds performed the best.** In 2019, the market risk appetite has picked up, and the higher-risk real estate bonds performed the best, with a total annual return of 13.63%, followed by financials (10.79%), sovereign bonds (9.83%) and non-financials (8.71%). Among them, except for non-financials bonds, real estate and financials high-yield bonds outperformed investment grade bonds. In addition, in the first half of 2019, the real estate, financial and non-financial bond returns were 9.56%, 7.26% and 6.61% respectively, while in the second half, the real estate, financial and non-financial bond returns were 3.53%, 3.22% and 2.00% respectively. The return of Chinese dollar bonds in the first half of the year was higher than that in the second half of the year, mainly due to the government's introduction of real estate and Chengtuo regulatory policies in June and July as well as the increased liquidity risk resulted from the continuous bond default, which led to the slowdown of Chinese dollar bond return in the second half of the year.

<sup>5</sup> Returns are calculated as  $[(\text{Index value at T1} / \text{Index value at T0}) - 1]$

**Exhibit 8: Returns of dollar bonds in 2019 by sector**

Markit iBoxx USD Asia ex-Japan China Index Return	H1	H2	2019
<b>Real Estate TRI</b>	9.56%	3.53%	<b>13.63%</b>
- Investment Grade TRI	7.74%	3.39%	<b>11.37%</b>
- High Yield TRI	10.55%	3.58%	<b>14.79%</b>
<b>Financials TRI</b>	7.26%	3.22%	<b>10.79%</b>
- Investment Grade TRI	5.76%	2.76%	<b>8.64%</b>
- High Yield TRI	9.49%	3.68%	<b>13.73%</b>
<b>Non-Financials TRI</b>	6.61%	2.00%	<b>8.71%</b>
- Investment Grade TRI	6.32%	2.89%	<b>9.33%</b>
- High Yield TRI	8.25%	-3.02%	<b>5.06%</b>
<b>Sovereigns TRI</b>	7.24%	2.49%	<b>9.83%</b>

Source: Bloomberg, CCXAP Research

## Rating Actions and Credit Events

The proportion of onshore negative rating actions decreased, while that of offshore negative rating actions was relatively high. In 2019, there were 371 issuer rating adjustment actions in the onshore market, and the number of downgrades was 150 times, accounting for 40.4% of the total actions, down 3.07 percentage points YoY. As the financing environment of private enterprise bond market has not been substantially improved, the downgrades were mainly concentrated in private enterprises, accounting for 78.5% of the total downgrades. From the perspective of sector distribution, the sectors with downgrades were widely distributed, including chemicals, non-ferrous metals, construction, investment, agricultural food processing and equipment manufacturing. There were 147 issuer rating adjustment actions in the offshore market in 2019, of which 96 were negative rating actions, accounting for 65.3% of the total actions, up 7.89 percentage points YoY, which mainly focused on real estate, Chengtou, industrial and consumer discretionary sectors.

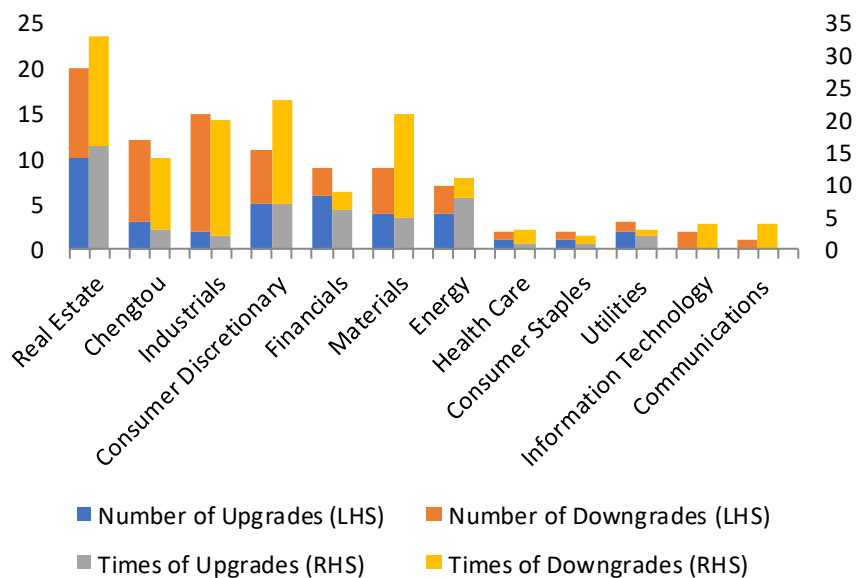
The number of real estate and Chengtou enterprises with rating being adjusted was the highest. In 2019, the three international rating agencies adjusted the issuer rating of 92 Chinese issuers, 21 fewer than in 2018, with 38 being upgraded and 55 downgraded. In terms of sector distribution, rating adjustments were mainly distributed in real estate, Chengtou and industrial sectors, involving 19, 12 and 15 issuers respectively. Among them, the numbers of real estate companies that have been upgraded and downgraded were 10 respectively<sup>6</sup>. The main reasons for upgrades are the improvement of financial profile and profit growth, while the main reasons for downgrades are the high leverage rate and tightened liquidity. In addition, the international rating agencies have downgraded 9 Chengtou enterprises, and only upgraded 3 Chengtou enterprises. Specifically, the negative rating action were mainly related to the downgrade of Government Related Entities (GRE)

<sup>6</sup> In 2019, a real estate company has been first downgraded and then upgraded.



as a result of the weakening of their financial strength. For example, four Tianjin Chengtou enterprises have been downgraded after Tianjin municipal government has been downgraded, which was mainly due to the slowdown of economic growth, counter-cyclical fiscal measures (such as tax reduction) and rising risks from GRE. On the contrary, the onshore rating agencies mainly upgraded the issuer rating of Chengtou enterprises. Specifically, there were 75 rating adjustments for Chengtou enterprises, including 72 upgrades and 3 downgrades. The upgraded Chengtou enterprises were mainly located in the relatively developed regions, and the reasons for the downgrade mainly included weak regional economic strength, poor profitability, and large short-term debt repayment pressure.

**Exhibit 9: Number and times of offshore rating actions by sector**



Source: Bloomberg, CCXAP Research

**Default events occurred frequently in the onshore market, and the default issuers were mainly private enterprises. The risk of individual credit events in the offshore dollar bond market may deserve more attention.** In 2019, the overall credit risk of onshore bond market remained at a high level, with 173 bonds defaulting, involving 65 issuers, with a total defaulted amount of RMB117.8 billion. The main reasons for default included the decline of industry prosperity, the contraction of financing channels, the decline of profitability, the excessive expansion of business and corporate governance. There were 38 new defaulting entities, 29 of which were private enterprises, accounting for 76.3%. This is because the downward pressure of the macro-economy in 2019 was still high, most of the private enterprises' own profitability has not been significantly improved, and their profit growth continued to be under pressure. However, the impact of onshore default events on offshore Chinese dollar bond market is relatively limited. In 2019, there were 9 Chinese enterprises with credit events in the offshore market, including Kangde Xin Composite Material Group

("KDX"), China Huiyuan Juice Group Ltd ("Huiyuan Juice"), China Minsheng Investment Group ("CMIG"), Qinghai Provincial Investment Group Co., Ltd ("Qinghai Provincial Investment"), Haikou Meilan International Airport Company Limited ("Meilan Airport"), Huachen Energy Co., Ltd. ("Huachen Energy"), Tewood Group Company Limited ("Tewood"), Tunghsu Group ("Tunghsu Group") and Peking University Founder Group Corp. ("Founder Group"). Generally speaking, credit events in offshore markets were all individual events, but the impact of individual credit events on the overall market may deserve more attention.

### Exhibit 10: Credit events of Chinese issuers in offshore market in 2019

Enterprise	Credit events
KDX	On January 15, Kangde Xin failed to pay "18 Kangde Xin SCP001", triggering a cross-default clause for the dollar bond that was guaranteed by the company and expired in 2020.
	On April 19, Kangde Xin announced that the company failed to raise sufficient funds during the 30-day grace period to repay the USD 300 million bond due in 2020, which constituted a material default.
Huiyuan Juice	On January 24, Huiyuan Juice announced that the company failed to redeem the convertible HKD bond due on January 23, which constituted a material default and triggered the cross-default clause of its dollar bond due in 2020. As of the end of 2019Q1, the company has not yet provided a debt solution.
	On February 19, Huiyuan Juice announced that it would delay the payment of interest on the dollar bond due in 2020. Since the bond has a 30-day grace period and the company completed payment on March 14, it did not constitute a material default.
CMIG	On January 29, the RMB 3 billion non-public targeted debt financing instruments issued by China Minsheng Investment expired. The company did not repay the principal on time and triggered cross-default clause of two dollar bonds due in 2019-2020, the keepwell agreements of which were provided by the company.
Qinghai Provincial Investment	On February 22, Qinghai Provincial investment failed to pay the interest of USD10.875 million on time. Because the bonds have a grace period of 5 working days, the Company has completed the payment on February 26, so it did not constitute a material breach of contract.
Meilan Airport	Haikou Meilan International Airport Co., Ltd., whose 35% of the shares are held by HNA Group, failed to pay the principal and interest payable of its USD200 million bond in full on September 6, 2019, which resulted in a default.
Huachen Energy	On November 18, 2019, Huachen Energy Co., Ltd. (Huachen Energy) failed to pay the interest of the USD500 million preferred notes issued on May 18, 2017 on the Singapore Stock Exchange on schedule. On December 18, 2019, the company announced again that 30 days have passed since the last interest due date, but the company still failed to pay the relevant payable interest, and its senior unsecured dollar bonds have constituted a default.
Tewood	On November 19, Tewood Group Company Limited ("Tewood") announced that the company could not pay the interest of USD500 million bonds due in 2020. December 1 is the interest payment date of the bond, and industrial and Commercial Bank of China, the issuer of the standby letter of credit, would pay USD7.875 million of interest on behalf of it. On November 22, Tewood put forward an exchange offer and redemption offer to four bondholders with a total amount of USD1.25 billion. The bondholders may choose to exchange some or all of the bonds into dollar bonds issued

by Tianjin State-owned Capital Investment Management Co., Ltd., or to resell them at a cash discount of 33% to 64%.

Tunghsu Group	On November 19, Tunghsu Optoelectronic Technology Co., Ltd. ("Tunghsu"), a subsidiary of Tunghsu group, failed to pay the interest payable and the related resale amount of its bonds on time due to the short-term liquidity difficulties. In addition, Tunghsu announced that the shareholders of Tunghsu Group planned to transfer their 51.46% shares to the State-owned Assets Supervision and Administration Commission of Shijiazhuang City. If the transaction is completed, it may trigger the cross default clause of Tunghsu group's dollar bonds.
Founder Group	On December 2, Peking University Founder Group Corp. issued a notice that as of December 2, 2019, the company failed to pay the principal and interest of bond "19 founder SCP002" in full on schedule. On December 23, Founder Group reached an agreement with its creditors to temporarily avoid cross default on its USD500 million bond.

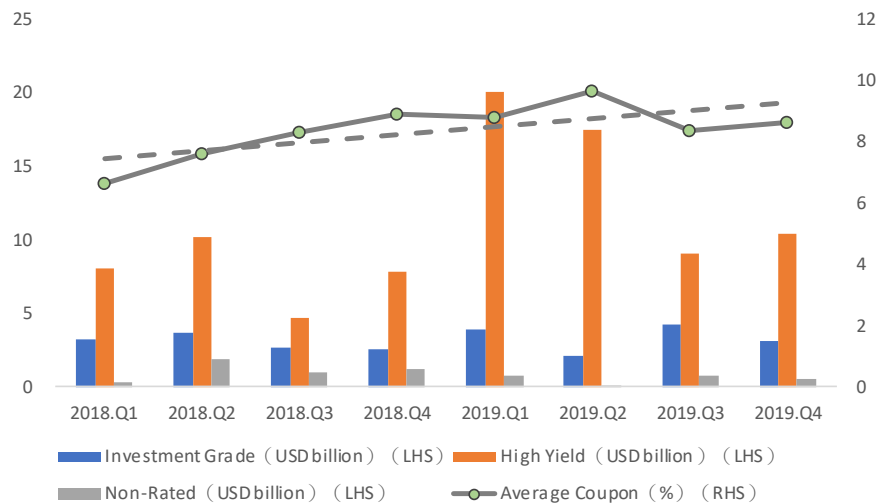
Source: public information, CCXAP Research

## Sector Overview and Development Trend

### *Real Estate Sector*

**In 2019, new issuance of Chinese real estate dollar bonds reached a record high, and the issuance rose first and then fell.** In 2019, 186 Chinese real estate dollar bonds were issued, with an amount of USD72.7 billion, up 44.2% and 50.3% YoY respectively. From the perspective of issuance pace, the issuance of Chinese real estate dollar bonds mainly focuses on the issuance window period at the beginning of the year, with the issuance amount of USD24.8 billion in the first quarter, accounting for about one third of the annual issuance. Subsequently, as the liquidity of real estate companies has become relatively abundant, the domestic land auction market has recovered. In order to prevent the land market from overheating, the regulatory agencies have successively launched regulatory policies, resulting in a tightening of the issuance of real estate dollar bonds, and the issuance from the second quarter to the fourth quarter has declined, with the issuance amount reduced to USD19.7 billion, USD14.1 billion and USD14.1 billion respectively.

As Chinese real estate dollar bonds were mainly high-yield issues, the average coupon rate showed a rising trend. In 2019, 153 dollar bonds were issued by high-yield Chinese real estate companies, with an amount of about USD57 billion, a significant increase compared with 86 and USD30.8 billion in 2018, resulting in an average coupon rate YoY increase of 113.6 basis points to 8.9%.

**Exhibit 11: New issuance of real estate dollar bonds in 2018 and 2019**

Source: Bloomberg, CCXAP Research

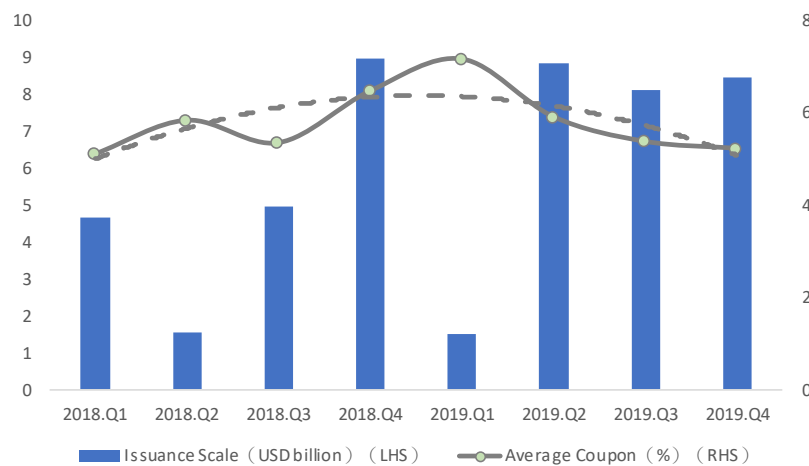
**The credit profile of real estate issuers continued to differentiate.** Because Chinese real estate companies mostly use high leverage to promote the rapid development of their own business, the credit rating of Chinese real estate companies was concentrated in the high-yield range of BB- to B-. After the rapid development of China's real estate sector, the development speed has slowed down significantly in the past two years, along with the regulatory policies in various regions, the capital mostly flowed to the large leading real estate companies instead of the smaller one, so the real estate sector showed a phenomenon of increased concentration and differentiation of credit profile. According to the issuer rating adjustments of three international rating agencies on Chinese real estate issuers, there were 16 upgrades and 17 downgrades of issuer rating in 2019 respectively. The main upgrades were the leading companies in the sector. After the rapid expansion of contracted sales, their revenues have gradually grown in the past two years. In addition, in the context of slowing industry growth, these real estate companies also began to control or lower the leverage level, which strengthened their credit profile. On the contrary, most of the downgrades were small and medium-sized real estate companies, whose sales and liquidity management have been weakened. Therefore, in the case of slowing industry growth and resources concentration in the leading companies, their cash-generating and refinancing abilities were limited, which leads to the liquidity problems of some companies and the weakening of credit profile.

### *Chengtou Sector*

**The new issuance of Chengtoug dollar bonds continued to grow, and many new issuers successfully issued bonds.** In 2019, 104 dollar bonds were issued by Chengtoug enterprises, with an amount of USD27.0 billion, up 40.5% and 38.6% YoY respectively. In the first quarter, the issuance of Chengtoug dollar bonds was small, which was about USD1.5 billion;

in the second to fourth quarter, the issuance was relatively stable, which were around USD8.5 billion. In order to prevent the foreign debt risk and the debt risk of local financing platforms, NDRC has issued Circular No. 666 in June to control the expansion of the Chengtou dollar bond market. However, since this Circular aimed at new Chengtou enterprises applying for the foreign debt issuance approval, there are no restrictions on the registered Chengtou enterprises, so there were still many new Chengtou enterprises issuing dollar bonds in the offshore market in 2019, supporting the issuance in the second to fourth quarter. In addition, among the 98 Chengtou issuers in 2019, 49 were new issuers.

**Exhibit 12: New issuance of Chengtou dollar bonds in 2018 and 2019**



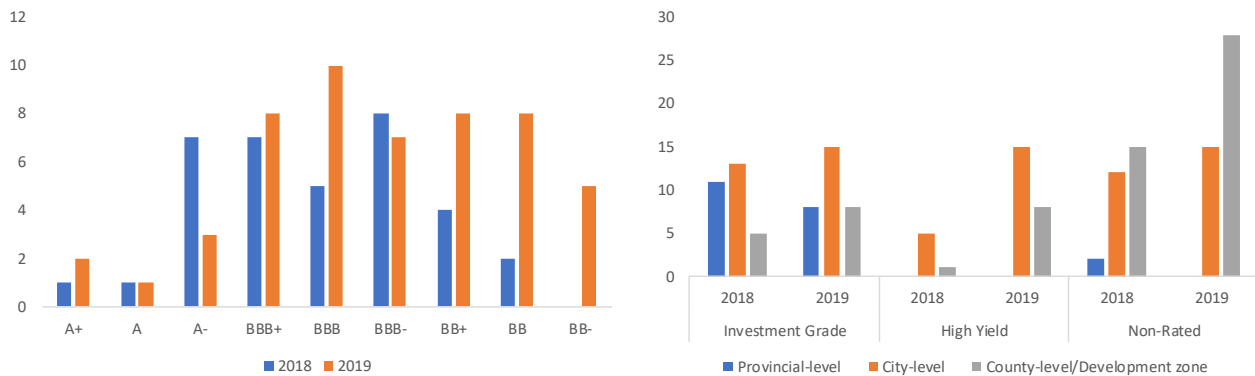
Source: Bloomberg, CCXAP Research

**The average coupon rate of Chengtou dollar bonds in 2019 was lower than that in 2018.** Although the credit profile of Chengtou issuers in 2019 was slightly weaker than that in 2018, due to the decline of US Treasury bond yields, the average coupon of Chengtou dollar bonds in 2019 was 33.9 basis points lower than that in 2018, reaching 5.6%. In addition, with the gradual recovery of investors' confidence in Chinese dollar bonds, the demand for Chengtou issuers with relatively good credit profile has increased, which also has a positive impact on the issuance coupon of Chengtou dollar bonds.

**The penetration of credit rating was serious for Chengtou issuers, high-yield bond issuers were active, and lower-tier issuers has appeared.** In 2019, there were 98 Chengtou dollar bonds issuers, 44 of which did not receive public credit rating from three international rating agencies, accounting for 44.9%. Most of these issuers were county-level or development zone-level Chengtou enterprises, and their credit profile were relatively average. Among the Chengtou issuers who have obtained the credit rating from the three international rating agencies, their ratings were mainly in the range of A+ to BB-, with investment grade being the majority, accounting for more than half of the issuers with public rating. Compared with 2018, the issuers' credit profile of Chengtou enterprises in 2019 has weakened. In 2018, there were 6 Chengtou bond issuers with public rating, accounting for about 17.1% of rated issuers; in 2019, the number and percentage rose to

23 and 42.6% respectively. In addition, county-level or development zone-level Chengtou issuers were active, and there were 44 county-level or development zone-level Chengtou issuers in 2019, an obvious increase compared with 21 in 2018. Compared with prefecture-level issuers, most county-level or development zone-level Chengtou issuers have relatively weak credit profile, which also led to a significant increase in high-yield issuers in 2019.

**Exhibit 13: Rating distribution of Chengtou issuers in 2018 and 2019**



Source: Bloomberg, CCXAP Research

## Outlook

**In 2020, in view of the refinancing demand of outstanding issuers, it is expected that the market of Chinese dollar bonds would continue to expand.** However, since NDRC issued Circular No. 666 and No. 778 in mid-2019 to prevent the rapid growth of offshore debt for Chengtou and real estate enterprises, we expect the effect of these two Circulars would be gradually reflected in 2020. As Chengtou and real estate enterprises are the major new issuers in the Chinese dollar bond market, the number of new issuers in 2020 may decrease compared with 2019. In terms of issuance pace, given the outbreak of coronavirus (COVID-19), the issuance peak would be postponed compared to 2019, with the issuance falling first and then rising. In terms of issuance cost, although the epidemic will curb the global economy in the near term, the negative impact on the economic growth throughout the year would be modest; and as the US Treasury yield remained low, the issuance cost of Chinese dollar bonds may have downward trend but with limited room. In terms of issuance tenor, Chinese issuers would still prefer 1 to 5-year medium-term dollar bonds; but as the yield spread between medium and long-term US Treasury bonds narrowed, more Chinese issuers (such as real estate companies) would consider to issue bonds with longer maturities to improve their debt structure, extending the average tenor of Chinese dollar bonds.

In terms of credit risk, with continuous downward pressure on China's economy in 2020, structural credit risk may be further exposed. The coronavirus outbreak would also weigh on the operations of some enterprises in the short term, so private enterprises with relatively weak credit profile would worth attention. In addition, the credit events of state-owned enterprises have increased in recent years. Considering that most of the state-owned enterprises issuing dollar bonds are of leading position in the sector, which have an important contribution to the national

or regional economic development, the overall credit profile of state-owned issuers is relatively good and the large-scale occurrence of credit risk events is less likely.

**We believe that China's real estate sector would continue to consolidate, and the credit profile of real estate companies would continue to diverge.** It is expected that the policymakers would adhere to the general direction of "housing is for living in, not for speculation", so the regulatory measures and financing policies for the property sector would be less likely to loosen significantly. Given the coronavirus outbreak, sales offices and agency offices in major cities have been closed, coupled with the delay of work resumption, resulting in the extension of project development cycle, pre-sale and payment collection cycle, as well as the heightening of financial pressure for some real estate companies. Overall, we believe that small and medium-sized real estate companies focusing on lower-tier cities and that with tight liquidity would be exposed to higher credit risk.

**We expect that lower-tier issuers for Chengtou dollar bonds would continue to emerge, but the overall credit risk would be under control.** The coronavirus outbreak has magnified the shortage of urban healthcare infrastructure and transportation network. It is expected that local governments would increase investment to overcome these shortcomings. As the vehicles for regional infrastructure investment and construction, Chengtou enterprises are likely to undertake these works, which would support their development opportunities in the future. On the other hand, the fiscal revenue of local governments would shrink in the short term, while the fiscal expenditure would surge to support the economic recovery, weighing on the financial performance of local governments. Therefore, we believe that the credit trend of Chengtou enterprises with weak financial strength and low administrative level would be closely monitored.

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