CCXI & CCXAP – Research & Commentary

High-Yield SOE Issuers Performed Well, Private Property Developers under Refinancing Pressure

Hong Kong, 25 October 2021 -- A report titled "High-yield SOE Issuers Performed Well, Private Property Developers under Refinancing Pressure: 2021Q1-Q3 Performance of High Yield Bond Index" has been recently published by the Research Institute of China Chengxin International Credit Rating Co. Ltd. ("CCXI Research Institute"). According to the report, High-yield bond market traded actively in the first three quarters of 2021 as sentiment repaired. The confidence in SOEs was regained, and risk-adjusted returns on high-yield LGFV bonds continue to lead. Since Q2, non-LGFV SOEs have shown outstanding performance with a rapid pickup in the net price index, suggesting that crisis-driven opportunities have been fully tapped by market participants. Wholesale retail and transportation saw underperformance amid the COVID-19 pandemic. Downward pressure on real estate industry intensifies as net price index closes down continuously. Going forward, special attention should be paid to the risk release from the tail end of private enterprises and volatile valuation risk of local LGFVs with weaker qualifications and the refinancing risk in the real estate industry.

CCXI High Yield Bond Index showed the following main characteristics in the first three quarters of 2021: First, by issuer, high-yield LGFV bonds had the best return/risk ratio, and the SOE index rose faster in Q3. In the first three quarters, high-yield LGFVs, non-LGFV SOEs and non-SOEs saw a cumulative yield of 5.37%, 5.09% and 1.64% respectively, with the LGFV bonds recording the highest overall return, lower volatility and drawdown and best return/risk ratio. Net price and wealth indices of high-yield non-LGFV SOEs have risen prominently since Q3, with the indices decreasing quarter by quarter and the risk-adjusted return second only to LGFV bonds. Non-SOEs generated poor yields with big drawdown and volatility and accelerating tail risk. **Second, by geography, the highest overall return on high-yield LGFV bonds went to Sichuan, Hunan and Zhejiang, with yields growing significantly in Tianjin in Q3.** High-yield LGFV bonds saw a positive return on wealth indices for all key regions in the first three quarters, with Sichuan, Hunan and Zhejiang leading the market with an overall return of 5.72%, 5.69% and 5.59% respectively. The net price indeces varied across regions, with Zhejiang, Hunan, Chongqing and Sichuan being top gainers of net price. As for relative performance in return and volatility, Jiangsu, Chongqing and Sichuan generally showed a higher return/risk ratio for high-yield LGFV bonds while Yunnan, Guizhou and Tianjin delivered weaker performance. However, Tianjin has seen a significant rise in return accompanied by lower volatility since the beginning of Q3. **Third, by sector, non-ferrous metals and coal led gains in a sectoral rotation, with real estate under growing downward pressure.** The high yield industry bond indices recorded a positive return except wholesale and retail in the first three quarters. Non-ferrous metals, light manufacturing, coal and financials led overall returns with 10.16%, 7.43%, 6.59% and 5.98% respectively. As for the net price indeces, non-ferrous metals and coal were top gainers in a rotation, securing remarkable capital gains.

The real estate industry registered a decline in the net price index for the third consecutive quarter, expected to remain under stressed liquidity conditions in Q4.

The report points out that, in the next stage, special attention should be paid to the risk release from the tail end of private enterprises and volatile valuation risk of local LGFVs with weaker qualifications and the refinancing risk in the real estate industry. The report points out that, **first,** the net price index of non-LGFV SOEs is expected to reach their peak as the net prices of non-LGFV SOE bonds rebounds with a declining trading activity in the secondary market. Non-SOEs have seen a week index with major drawdown and volatility, showing a notable drop in primary-market refinancing. Special attention should be paid to risk release from private enterprises at the bottom rung going forward. **Second,** as for high-yield LGFV bonds, some debt-ridden regions with weaker financial strengths and reliant heavily on government fund revenue may be under great funding pressure. The bond price may become more volatile, and valuation risk arising from the regional spread of default on non-standard securities and guarantee payout risk should be guarded against. **At last,** as for high-yield industry bonds, as the real estate curb policy is tightening, the negative credit events of some medium-sized and large private developers have further battered investor confidence. The real estate industry is expected to remain under stressed liquidity conditions as developers have much less access to external financing, coupled by continued slowdown in property sales. Overall, the downward pressure on real estate still shows no signs of material abating. Investors are advised to wait for the turning point and adopt a right-side gaming model.

To obtain the full report, please call our Customer Service Hotline +852-2860 7111.

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