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SECTOR COMMENT
6 October 2020

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Property – China

Regulators will maintain control over property developers' access to debt funding

This report is excerpted from Top of Mind: Frequently asked questions about top global sectors

Do you expect Chinese regulators will announce new measures to control Chinese property companies' debt leverage?

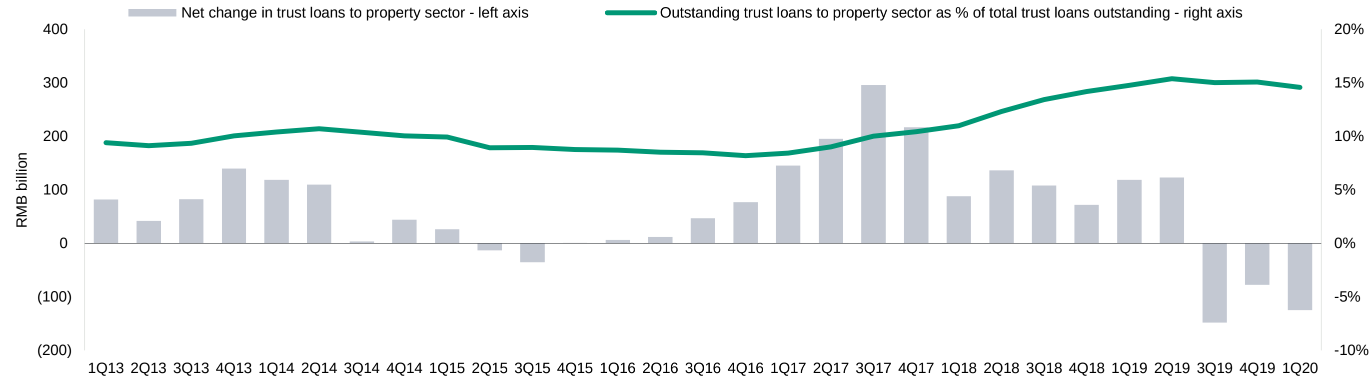
Yes, we do expect Chinese regulators will continue to implement and fine-tune regulatory measures to control Chinese property developers' debt-funding access and consequently their debt leverage. This control is aimed at maintaining stability in the country's property sector given the important role it plays in China's economic growth.

Most recently, regulators have reportedly implemented new debt-growth controls with a dozen large developers and could extend them to a larger group of developers, according to media reports. The controls apply to short-term liquidity, capital adequacy and overall debt levels, according to the media reports. To date, there is no official government announcement.

Regulators also exerted significant control last summer when they tightened the restrictions on developers' offshore bond issuance. China's National Development and Reform Commission issued a notice on its website in July 2019 that included the following requirements: developers must use the proceeds from offshore bond issuance only to refinance offshore bonds with tenors of more than one year that are maturing in the coming 12 months; explain the purpose of the offshore bond issuance in the prospectus; and control risk around foreign-currency debt.

These requirements came two months after the China Banking and Insurance Regulatory Commission tightened developers' access to trust loans, as part of the government's continued efforts to clamp down on shadow banking. Issuance of new trust loans to the property sector is likely to decline moderately in the next 12 months because of the tight regulatory control over shadow bank financing (Exhibit 1).

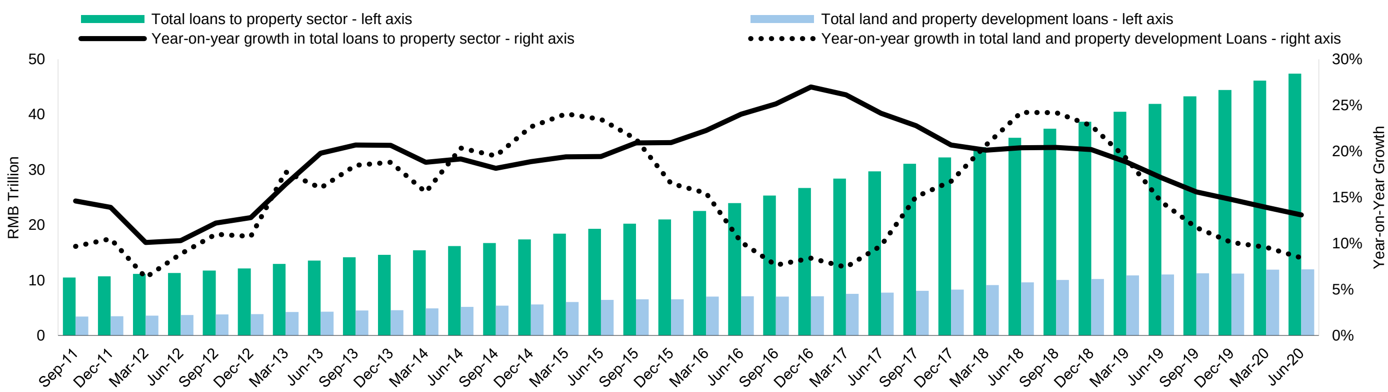
Exhibit 1
Trust lending to the property sector is declining



Sources: Wind Information Co. and Moody's Investors Service

We also expect bank lending growth to developers will continue to slow because regulators will selectively control credit growth to limit developers' debt growth, especially developers with already high leverage (Exhibit 2).

Exhibit 2
Bank lending growth to the property sector is slowing
Year-on-year growth



Total loans to property sector include land and property development loans and mortgage loans.
Sources: The People's Bank of China, National Bureau of Statistics and Moody's Investors Service

China's property market is large and fragmented with thousands of developers, most of which are small. We rate 70 developers, which are among the largest in China. The rated developers' leverage, as measured by revenue/adjusted debt, has remained largely stable for the 12 months ended June 2020 compared with full-year 2019.

We expect it to improve moderately during the next 12-18 months. The improvement will be driven by higher project completion and revenue recognition during the second half of this year and in 2021, coupled with developers' controlled debt growth. The latter reflects the regulatory control of the sector's leverage.

Regulators also control the physical property market. On 30 July, China's central government reaffirmed its commitment to the stability of the property market amid increasing property prices at a meeting held by the Central Political Bureau of the Communist Party of China. The People's Bank of China (PBOC) also stated on its website that it, together with the housing ministry, reiterated at a conference held with some developers on 20 August that China would not use the housing market as a short-term stimulus to support the economy and would continue to stabilize land prices, home prices and property market expectations. Additionally, the PBOC stated that it and the housing ministry would jointly strengthen the monitoring of the financing activities of major developers.

We expect local Chinese governments will continue to implement and adjust regulatory measures as needed to prevent sharp property-price increases. They have done so in response to price increases in some Tier 1 and Tier 2 cities over the past six to nine months.

We expect property prices will rise just slightly during the next six to 12 months as the government continues to implement regulatory controls, including control of credit growth, to prevent a run-up in property prices and to foster the long-term stable development of China's property market.

REPORT NUMBER 1244362

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