

China Property Sector

Banks may have to bail out some troubled projects

The property crisis finally turned into an alarming event after a rapidly rising number of house buyers refused to pay mortgage for the unfinished projects of developers. With so many developers under distress or default, we calculated the total GFA of construction halt could be as many as 630mn sqm or 6mn units (11% of total construction and 86% of 2021 completed GFA). If this goes further viral, we think it may again hurt the already-fragile primary sales market on the delivery risk. By then even high quality names like Longfor may be under huge stress as buyers may not be rational enough to tell. The short-term solution has to rely on the bailout by banks and local government based on our channel check. However, we think the banks will be selective to choose almost-finished projects so they can benefit most (that means mortgage >> costs to finish projects)

- **What is new:** [According the ifeng, over 50k primary house buyers have announced to reject paying mortgages as the projects they bought have halted construction for long and faced the risk of being never finished.](#) These troubled projects in the news are mainly developed by Evergrande, Sinic, Greenland and other defaulted names located in 12 cities including Zhengzhou, Wuhan and Changsha.
- **What is the potential size of unfinished projects?** The trigger point for such massive construction halt is due to pre-sales fund being used illegally by some developers, which then faced liquidity issue and debt default after big sales decline. Based on our calculation, 23 developers are defaulted among Top 100 names and they have recorded RMB6.3tn sales in 2020 and 2021 which are due to be delivered in 2022/2023. If we assume all these projects are into some troubles, this would mean there could be as many as 630mn sqm of GFA construction halted, which is 11% of total GFA under construction or 86% of 2021 completed GFA. Also, we think the unfinished GFA as % of sales is also getting much higher as we calculated completed GFA/new starts (3 years ago) ratio and see the huge decline from 100% (almost all delivered) to latest 48% in 2021 (the new low).
- **What is the potential solution?** As the event is spreading very quickly across the whole country, we think MOHURD, PBOC and local governments would step in to provide some bailout based on our channel check. The likely solution in the near term is that banks, as the only entity who has liquidity to support and could benefit, may provide bailout money to help finish the project, so that they can still get mortgage paid. However, the bailout will be selective to achieve two objects: 1) social stability which means as many as possible house buyers could see their house finished. 2) Economically viable which means that banks may only select projects with the total mortgage payments >> the construction costs so they can cover much more than what they pay. For example, one project is short of RMB100mn cash to be finished and house owners owe banks RMB10bn for the mortgage. We think banks may have the motivation to provide bridge loans to help finish this project so they still get RMB900mn back and then try to recover RMB100mn from the developer.
- **What is the sector implication:** this may further hurt the sales sentiment especially for primary market. Even quality non-SOE developers like Longfor or CIFI may face buyers' concerns on home delivery given the overall low confidence. This could even push more demand into secondary market which has no delivery risk and we have indeed seen much more resilient secondary sales (positive YoY in consecutive 5 weeks) than primary market. (Figure 3 and 4).

OUTPERFORM
(Maintain)

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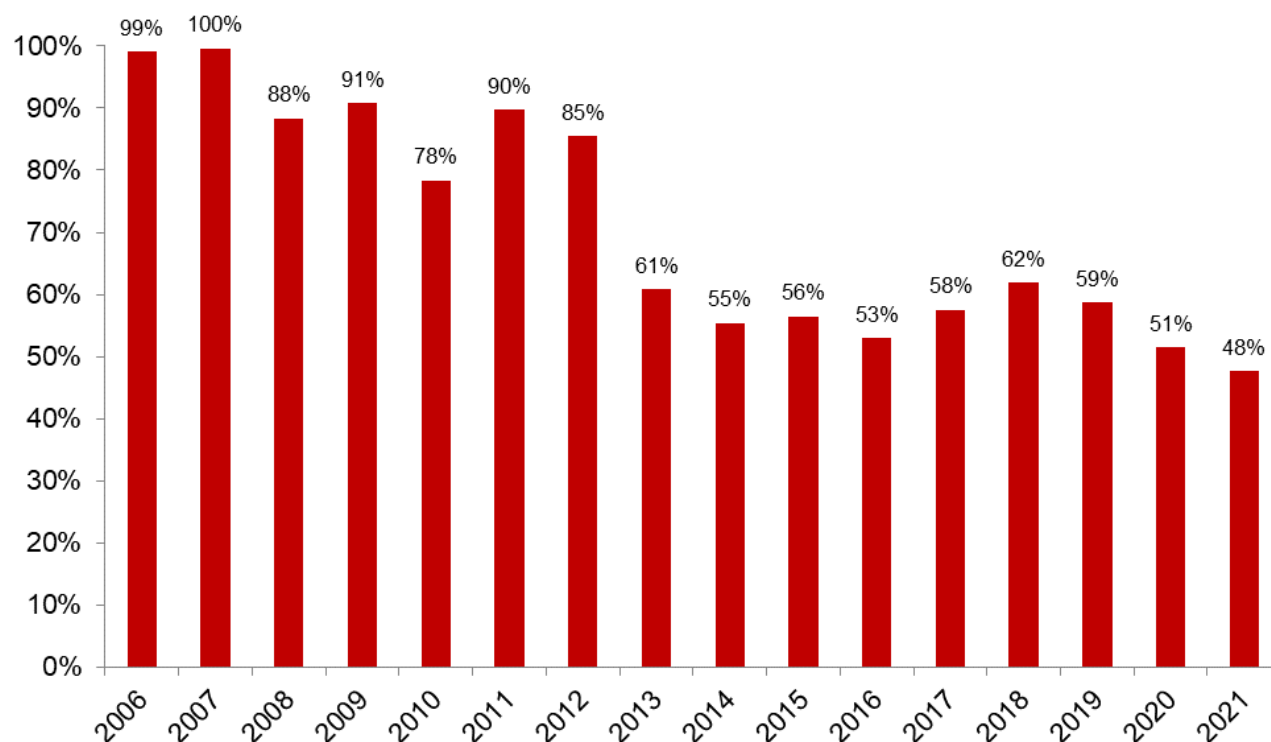
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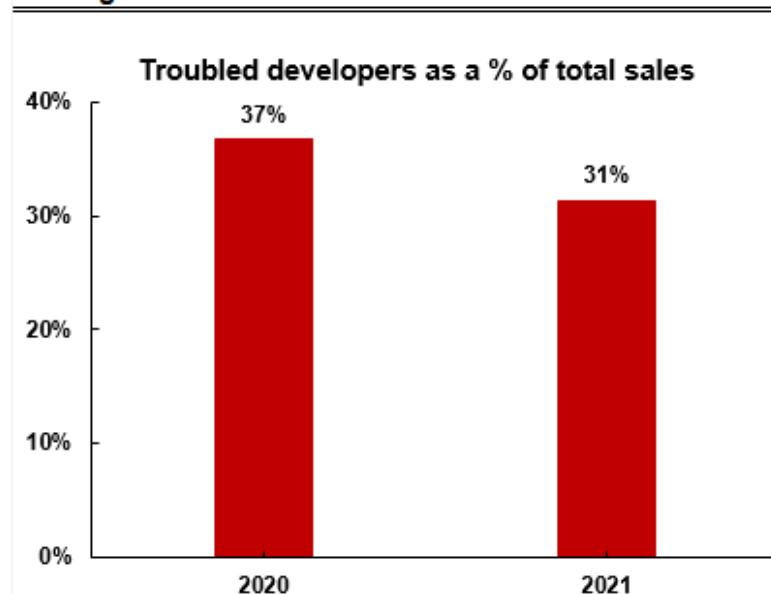
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Figure 1: Residential completion to residential starts 3 yrs earlier

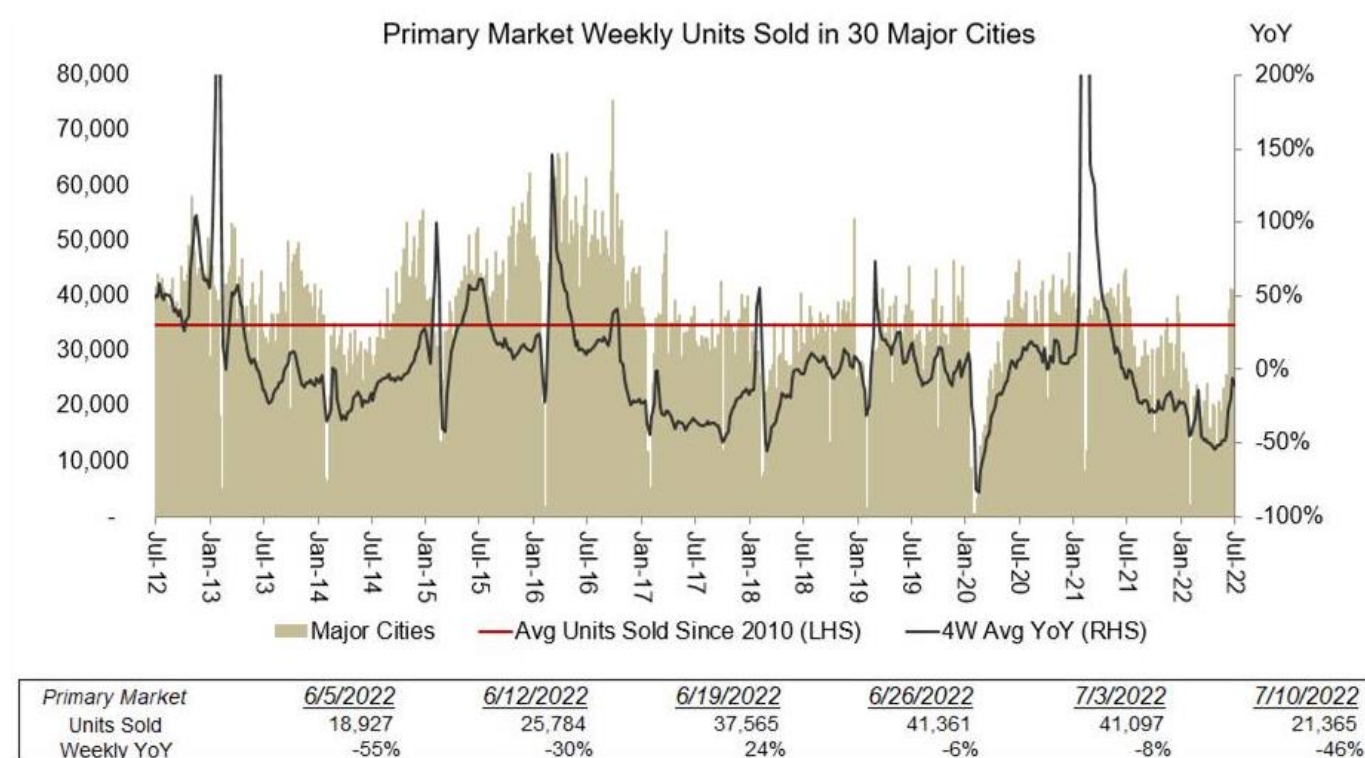
Source: NBS, CMBIGM

Figure 2: Troubled developers as a % of total sales

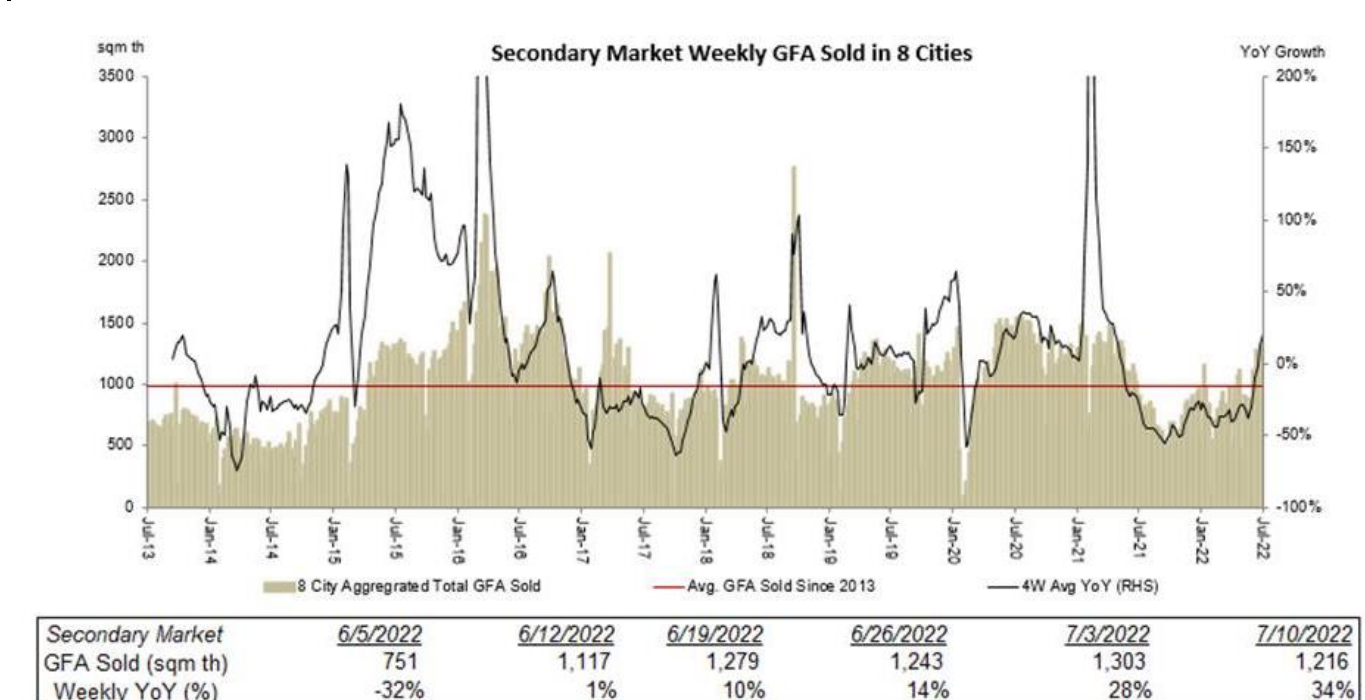
Top 100 Developers' Annual Attributable Sales Value (RMB Bn)			
Troubled Developers	Total	as % of total	
2020	34,708	94,462	37%
2021	27,826	88,716	31%
Average			34%



Source: Company, CRIC, CMBIGM

Figure 3: Primary sales in 30 cities

Source: Wind, CMBIGM

Figure 4: Secondary sales in 8 cities

Source: Wind, CMBIGM

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