CMBI Credit Commentary

LGFVs: Our thoughts on the plan to purchase unsold residential units

Glenn Ko, CFA 高志和
(852) 3657 6235
glennko@cmbi.com.hk

Cyrena Ng, CPA 吳蒨瑩
(852) 3900 0801
cyrenang@cmbi.com.hk

Jerry Wang 王世超
(852) 3761 8919
jerrywang@cmbi.com.hk

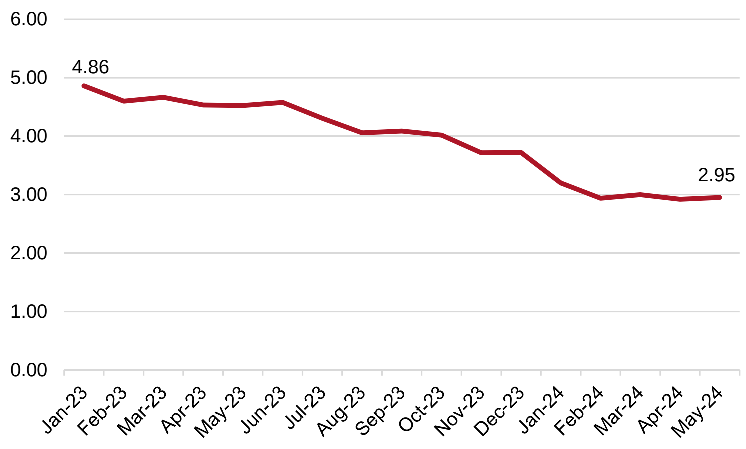
A move in the right direction to address high inventory level

Media reported Chinese government's plan to have local governments to purchase unsold residential units and convert these to affordable housings. While there remains a high level of uncertainty as to the timing and details of implementation, we believe that the reported plan helps address one of the key obstacles in restoring homebuyer's confidence, i.e. growing inventory level, through turning inventory into affordable rental housing to meet the demand from lower-income groups. As we discussed before, the Chinese property market is in a vicious cycle with falling price and higher inventory level. Ensuring timely deliveries of pre-sold projects, lower inventory level and stabilized property prices are keys to restore confidence on the property market.

How will the plan be implemented and what will be the sources of funding for local governments?

The plan in the brewing is not entirely new. Indeed, local governments of Fuzhou, Chongqing, Zhengzhou and Suzhou had acquired unsold residential units and convert these into social housings. On 14 May'24, the Housing and Urban-Rural Development Bureau of Linan District of Hangzhou offers to acquire completed residential units (and car parks) at market prices for social rental housings. Taking cues from the experience of Zhengzhou, the LGFVs there acquired unsold residential units at discounts, primarily funded with bank loans, and convert these units to social rental housings. The funding cost of these acquisitions is lower than the rental yield. We believe that opening up long-term and low-cost funding channels including onshore loan and bond markets for LGFVs are keys to the success of this plan.

Coupon rate movement of LGFV onshore bonds (%)



Source: Wind.

CMBI Fixed Income
fis@cmbi.com.hk

Impact to LGFVs: Neutral to positive

There may be concerns on the sources of funding for local governments and additional financial burden of LGFVs. However, as discussed before, we believe that LGFVs will only acquire projects at prevailing market prices under heavy regulatory scrutiny and LGFVs will be granted the access to long-term and low-cost funding channels in the acquisitions of unsold residential units. We also believe that these could open new and recurring income sources for LGFVs involved, as well as strengthen their strategic importance within their respective regions. In our opinion, LGFVs more likely to involve in the plan are those with experience in property and social housing sectors such as **CPDEV** and **ZHHFGR**.

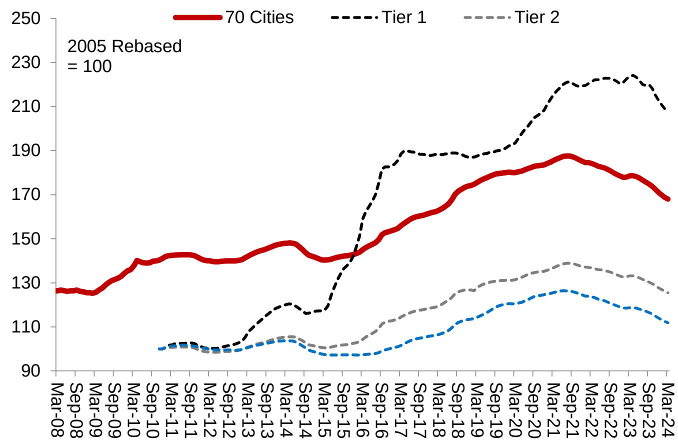
Impact to the property developers: Mixed

The move sent another signal that the Chinese government's strong intention to stabilize the property market. The reported move is positive to developers in general. Nonetheless, the impact to individual developers in the near-term will vary. For developers already in default with a high inventory level, they may be pressured to sell projects to local governments/LGFVs at deep discounts. These could affect the overall recovery value, especially from offshore bondholders' perspective.

General inventory month

Source: Wind.

NBS 70 cities ASP (2nd-hand) index



Source: Wind.

CMB International Global Markets Limited

Fixed Income Department
Tel: 852 3657 6235/ 852 3900 0801
fis@cmbi.com.hk

Author Certification

The author who is primary responsible for the content of this research report, in whole or in part, certifies that with respect to the securities or issuer that the author covered in this report: (1) all of the views expressed accurately reflect his or her personal views about the subject securities or issuer; and (2) no part of his or her compensation was, is, or will be, directly or indirectly, related to the specific views expressed by that author in this report.

Besides, the author confirms that neither the author nor his/her associates (as defined in the code of conduct issued by The Hong Kong Securities and Futures Commission) (1) have dealt in or traded in the stock(s) covered in this research report within 30 calendar days prior to the date of issue of this report; (2) will deal in or trade in the stock(s) covered in this research report 3 business days after the date of issue of this report; (3) serve as an officer of any of the Hong Kong listed companies covered in this report; and (4) have any financial interests in the Hong Kong listed companies covered in this report.

Important Disclosures

There are risks involved in transacting in any securities. The information contained in this report may not be suitable for the purposes of all investors. CMBIGM does not provide individually tailored investment advice. This report has been prepared without regard to the individual investment objectives, financial position or special requirements. Past performance has no indication of future performance, and actual events may differ materially from that which is contained in the report. The value of, and returns from, any investments are uncertain and are not guaranteed and may fluctuate as a result of their dependence on the performance of underlying assets or other variable market factors. CMBIGM recommends that investors should independently evaluate particular investments and strategies, and encourages investors to consult with a professional financial advisor in order to make their own investment decisions.

This report or any information contained herein, have been prepared by the CMBIGM, solely for the purpose of supplying information to the clients of CMBIGM and/or its affiliate(s) to whom it is distributed. This report is not and should not be construed as an offer or solicitation to buy or sell any security or any interest in securities or enter into any transaction. Neither CMBIGM nor any of its affiliates, shareholders, agents, consultants, directors, officers or employees shall be liable for any loss, damage or expense whatsoever, whether direct or consequential, incurred in relying on the information contained in this report. Anyone making use of the information contained in this report does so entirely at their own risk.

The information and contents contained in this report are based on the analyses and interpretations of information believed to be publicly available and reliable. CMBIGM has exerted every effort in its capacity to ensure, but not to guarantee, their accuracy, completeness, timeliness or correctness. CMBIGM provides the information, advices and forecasts on an "AS IS" basis. The information and contents are subject to change without notice. CMBIGM may issue other publications having information and/ or conclusions different from this report. These publications reflect different assumption, point-of-view and analytical methods when compiling. CMBIGM may make investment decisions or take proprietary positions that are inconsistent with the recommendations or views in this report.

CMBIGM may have a position, make markets or act as principal or engage in transactions in securities of companies referred to in this report for itself and/or on behalf of its clients from time to time. Investors should assume that CMBIGM does or seeks to have investment banking or other business relationships with the companies in this report. As a result, recipients should be aware that CMBIGM may have a conflict of interest that could affect the objectivity of this report and CMBIGM will not assume any responsibility in respect thereof. This report is for the use of intended recipients only and this publication, may not be reproduced, reprinted, sold, redistributed or published in whole or in part for any purpose without prior written consent of CMBIGM.

Additional information on recommended securities is available upon request.

Disclaimer:

For recipients of this document in the United Kingdom

This report has been provided only to persons (I)falling within Article 19(5) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 (as amended from time to time)("The Order") or (II) are persons falling within Article 49(2) (a) to (d) ("High Net Worth Companies, Unincorporated Associations, etc.,) of the Order, and may not be provided to any other person without the prior written consent of CMBIGM.

For recipients of this document in the United States

CMBIGM is not a registered broker-dealer in the United States. As a result, CMBIGM is not subject to U.S. rules regarding the preparation of research reports and the independence of research analysts. The research analyst who is primary responsible for the content of this research report is not registered or qualified as a research analyst with the Financial Industry Regulatory Authority ("FINRA"). The analyst is not subject to applicable restrictions under FINRA Rules intended to ensure that the analyst is not affected by potential conflicts of interest that could bear upon the reliability of the research report. This report is intended for distribution in the United States solely to "major US institutional investors", as defined in Rule 15a-6under the US, Securities Exchange Act of 1934, as amended, and may not be furnished to any other person in the United States. Each major US institutional investor that receives a copy of this report by its acceptance hereof represents and agrees that it shall not distribute or provide this report to any other person. Any U.S. recipient of this report wishing to effect any transaction to buy or sell securities based on the information provided in this report should do so only through a U.S.-registered broker-dealer.

For recipients of this document in Singapore

This report is distributed in Singapore by CMBI (Singapore) Pte. Limited (CMBISG) (Company Regn. No. 201731928D), an Exempt Financial Adviser as defined in the Financial Advisers Act (Cap. 110) of Singapore and regulated by the Monetary Authority of Singapore. CMBISG may distribute reports produced by its respective foreign entities, affiliates or other foreign research houses pursuant to an arrangement under Regulation 32C of the Financial Advisers Regulations. Where the report is distributed in Singapore to a person who is not an Accredited Investor, Expert Investor or an Institutional Investor, as defined in the Securities and Futures Act (Cap. 289) of Singapore, CMBISG accepts legal responsibility for the contents of the report to such persons only to the extent required by law. Singapore recipients should contact CMBISG at +65 6350 4400 for matters arising from, or in connection with the report.