Chinese business & finance

Chinese bad debt exchange opens channel to foreign investors

Shenzhen-based QEX first to open onshore NPL market to global fund managers

Don Weinland in Hong Kong AUGUST 29, 2018

China's largest financial asset exchange is increasing sales of bad debt to overseas investors in the country's latest attempt to find new buyers for its expanding pool of non-performing loans.

The Rmb1tn ($147bn) market, called the Qianhai Financial Assets Exchange, was launched by the Shenzhen government in 2011 and bought out by Ping An Group in 2015. Last year it became the first exchange to begin selling bad debt directly to overseas buyers.

Its deputy general manager Zhan Yuhong said he expects the volume of foreign sales to double this year compared with 2017 to more than Rmb10bn.

Regulators this year are forcing banks to recognise vast stores of once-hidden unpaid debts. However, monetary tightening in the country has limited the amount of domestic funds available to buy up those credits as they come on to the market.

One answer has been to make it easier for foreign investors to access China's onshore market for bad debt, a notoriously difficult area of investment fraught with legal opacity.

"There is not enough demand in China for the debt coming on to the market. Liquidity at all institutions has shrunk this year," said Mr Zhan. "This is why the government is promoting selling NPLs to overseas investors. This is one of the solutions."

1.86%

Chinese banks' ratio of non-perfoming loans

The exchange processed Rmb1tn in transactions last year, the vast majority of which were domestic. In the first half of 2017 it sold about Rmb5bn to foreign investors after launching a pilot programme early last year that allowed it to market to global fund managers.

The QEX is one of a handful of financial assets exchanges that have appeared across the country over the past decade and deals primarily in bad debt. On the QEX website investors can sift through pages of individual credits for Chinese companies in distress.

Transferring bad loans to government-controlled asset management companies has been the leading means to relieve the banks of bad loans for more than a decade. These asset managers have also become the primary sellers of the debt to foreign investors.

The QEX hopes to become a new channel into the market by simplifying and shortening the process for foreign investors, Mr Zhan said. Once a deal is agreed, the QEX can close it within two to three weeks, he said; an asset management company can take several months.

“The big four [asset management companies] are actually not that interested in doing transactions with foreign investors because it takes too long,” said Zhang Xiaolian, a partner at King & Wood Malleson in Beijing, who is currently working on two QEX sales to foreign buyers.

The challenge of the QEX model is that the small number of foreign investors who already have experience in the Chinese bad debt market have tried and tested means of buying the debt directly from asset managers and some are reluctant to seek out new channels, she said.

Three foreign investors active in the market said they preferred to deal directly with sellers in order to get better pricing. The simplified exchange process means more investors will have access and therefore prices are expected to be higher, they said.

Link: https://www.ft.com/content/033d94ac-ab61-11e8-94bd-cba20d67390c