



10/04/2021

## FUSCO FINANCIAL ASSOCIATES

Market Commentary

To Our Valued Clients,

Some weeks present a bit of a challenge when finding appealing topics to write about for market commentary purposes, last week was certainly not one of those weeks. We had the Senate voting on bills to suspend or extend the debt ceiling, the debate surrounding the infrastructure and economic spending packages, and the UK beating its 2<sup>nd</sup> quarter GDP estimates by nearly 15%, to name a few. While we are closely monitoring all of these developments I would like to direct our attention to a topic that a handful of our clients have reached out to us on over the past couple of weeks, China's troubled real estate company, Evergrande Group.

With nearly 150,000 employees, \$316B in total assets, and 1,300 ongoing projects, Evergrande is not only one of China's largest companies but ranks amongst the top 250 largest in the world, according to Forbes<sup>1</sup>. Specializing in residential real estate development, the company has primarily financed its ventures through debt, issuing onshore and offshore bonds to the tune of \$300B by September of this year<sup>2</sup>. These debt issues carried a Fitch rating anywhere from a BB+ in the earlier years down to C ratings more recently. With issues spanning both the speculative and junk bond categories, Evergrande debt carries a steep interest rate, up to 9.5% in some cases<sup>3</sup>. The indebted firm began to run into trouble in 2020 as COVID-19 impacted cash flows, significantly straining its ability to make lofty interest payments to bondholders. After staying afloat through Q2 of this year, murmurs of a default began back in July and have only grown since. With the sheer size of Evergrande's outstanding debt being the equivalent of ~2% of China's GDP, contagion fears began to mount as investors pondered the impact a potential default would have on the global economy. Many have gone as far to say that this going to be another "Lehman moment." While the size of the two companies is comparable, some important differences that have the potential to dampen significant contagion. For starters, the Evergrande debt exposure is primarily held by Chinese mutual funds, private investment funds, and private companies. This is a stark difference from Lehman whose bad debt was mostly held by other investment banks which, by nature, are highly intertwined with the global financial system. Secondly, of the \$300B in debt,

---

<sup>1</sup> Forbes Global 2000

<sup>2</sup> Caixin

<sup>3</sup> Fitch Ratings

only \$19B exposure is held internationally. Evergrande also has ample real assets in the form of land, equipment, and ongoing projects. All of which can be liquidated in an attempt to make good on their interest payments.

Evergrande has already missed two offshore interest payments, and the likelihood of continued missed payments is high. A very bad situation for anyone holding their debt, a likely threat to the growth of China's economy, but not a significant threat to the global economy at this point. Thanks for reading, and as always, if you have any questions, or if we can help in any way, please don't hesitate to give our office a call.

With My Best Regards,

*Brandon Hethcoat*

Brandon Hethcoat

Investment Strategist

Registered Representative, RJFS



505 Baltimore Ave.  
Towson, MD 21204  
(410) 296-5400

---

3825 Leonardtown Rd., Suite 6  
Waldorf, MD 20601  
(301) 710-5880

---

Visit us at [www.fuscofinancial.com](http://www.fuscofinancial.com)

Securities offered through Raymond James Financial Services, Inc., member FINRA / SIPC. Investment advisory services offered through Raymond James Financial Services Advisors, Inc. Fusco Financial is not a registered broker/dealer and is independent of Raymond James Financial Services, Inc.

Any opinions are those of Fusco Financial Associates and not necessarily those of Raymond James. This material is being provided for informational purposes only and is not recommendation. There is no guarantee that these statements or opinions will prove to be correct. Investing involves risk and you may incur a profit or a loss regardless of strategy selected. Prior to making an investment decision, please consult with your financial advisor about your individual situation.

The stock indexes mentioned are unmanaged and cannot be invested into directly. Past performance is no guarantee of future results.