It's Oh So Grand.

Dr. Evil is paying particular attention to Shenzhen based Evergrande Group, the PRC's largest property developer. Wait a minute…property developers in a country where the State owns all the property? Communist landlords? How can that be? Dr. Evil loves contradictions. In any event, Evergrande's a mess with $122B in debt…

Evergrande Debt Continues to Pile Up Amid Cash-Flow Concerns: Bloomberg News: 31 AUG 2020:

The company's total debt edged up 4% to 835 billion yuan ($122 billion) at the end of June, compared with 800 billion yuan at the end of 2019, according to the earnings report released Monday by the Shenzhen-based company. The company said earlier this month that first-half net income including minority interests fell 46% to about 14.7 billion yuan. Profit attributable to shareholders plunged 56% to 6.5 billion yuan.

and corporate Attention Deficit Disorder, trying to recreate itself as an electric vehicle company and a healthcare company…and whatever sells paper (stock, bonds, whatever). Can you say amateur?

China's Evergrande Unveils Six New Energy Vehicles, Ushers in Leap-forward Development in NEVs: PandaDaily: Ella Cao: 4 AUG 2020: "…Evergrande's three-year investment budget in the field of NEVs totals 45 billion yuan, of which 20 billion was invested in 2019, 15 billion will be invested in 2020, and 10 billion will be invested in 2021. [If they're still in business.] Formally deemed as an amateur in the NEV industry, the Hong Kong-listed Evergrande stated in its announcement on July 27 that since the company is shifting its mainline business to the field of NEVs, the board of directors proposed to change its name to China Evergrande New Energy Vehicle Group Limited, which can be referred to as Evergrande Auto."

…Is perpetually 'deleveraging' but never actually gets deleveraged.
China's Evergrande plans to sell bulk of commercial properties: Reuters July 09, 2020:

Bleeds cash, discounts its real estate margin by 25% just to sell, while its' net income drops like rock..
Evergrande reports 54% fall in 2019 net profit: ChinaDaily: Pamela Lin: 01 APR 2020:

"Chinese real estate giant Evergrande Group on Tuesday reported a fall of about 54 percent in its net profit in 2019. In response to the pandemic, Evergrande offered a 25 percent discount for all property sales in February on its app, and the discount was narrowed to 22 percent in March."

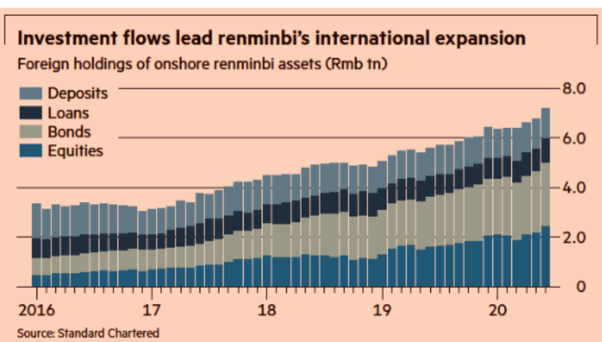
Sells dodgy 'naked' [no legal guarantees] bonds through the British Virgin Islands to yield hunger investors who are depending upon a communist regime to insure their investment…Communists & Western Investors…it's a fiscal love tussle...

CHINA EVERGRANDE TESTS THE "TOO BIG TO FAIL" HYPOTHESIS WITH $1B BOND SALE AT 11% : Mingtiandi.com -Asian Real Estate Intelligence: Jan Kot 20 SEP 2018 "Issued through a British Virgin Islands entity called Scenery Journey, the bond uses a covenant structure which includes its onshore subsidiary Hengda Real Estate Group providing a so-called "keepwell" deed to maintain the issuer's solvency, without offering a formal guarantee. These deeds have proliferated in China's bond market in recent years but they are largely untested, according to the industry source.

The lack of security for Evergrande's creditors appears to fit with a generally erosion in bond covenants in the region, with Moody's Investors Service stating this week that covenant quality for Chinese developer bond had fallen to its all-time weakest level, according to a recently completed survey by the credit rating agency.

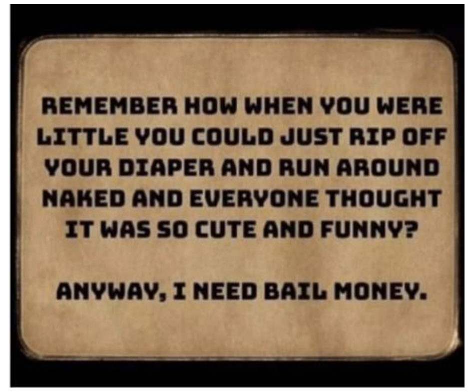
>>Yes, Dr. Evil is quite aware that article was from 2018, but western investors have gotten progressively dumber since then…and China is sucking up western capital with yields significantly higher than the US and Europe…

Demand for Chinese bonds boosts renminbi's global role: Financial Times [Paywall]: Eva Szakay, Hudson Lockett: 8 OCT 2020: " Foreign investors are snapping up Chinese debt, lured by relatively high yields and the country's strong economic recovery from the pandemic, with record demand likely to boost efforts to develop a global role for the renminbi." Investors can earn a **yield of about 2.7 per cent** on **10-year Chinese government debt** compared with **less than 0.8 per cent on the equivalent US Treasury**. [that's 3.37x for you math majors] Flows into China's onshore bond markets in the year to August topped Rmb615bn ($90bn), bringing foreign holdings to Rmb2.8tn. Net equity market inflows were Rmb93bn for the same period, taking foreign holdings to more than Rmb1tn. "The inclusion of Chinese assets into major bond and equity indices is a very strong indication of the PBoC's intentions around . . . the renminbi and it clearly tells us that the central bank wants to move more towards liberalizing its markets," said Gaurav Mallik, chief portfolio strategist at State Street Global Advisors.[When you think of Chief Portfolio Strategists….think of really annoying used car dealers…they're just sell side 'analysts' who've crammed client accounts and ducked SEC violations long enough to get seniority.]



Chief Portfolio Strategist

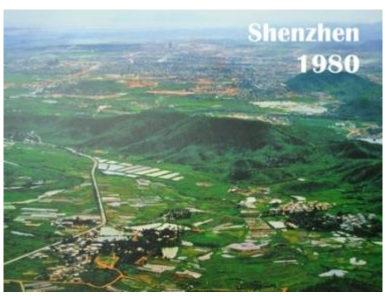
So why does Dr. Evil care about Evergrande Group? Because it sits, like Jabba the Hut, at the nexus of China's licit banking & shadow banking, fundamental investing & speculative, momentum investing. It is a canary [*albeit a giant bloated carnivorous canary*] in the PRC's coal mine of a consumer financial system. The answer to why it sits there at all involves property and rates of return. Property -All land in China belongs to the State…just ask them. The State [Bejing, Provincial or township] taketh and it giveth. If the State needs money, they take property from peasants [*"hey guys, you're taking this ancestral thing a little too far. So, you've been here for 2 thousand years…So what…Times change… Open fire"]* and give it to developers who promise greater tax revenues…and maybe some kickbacks [*nah…did I say that?!*]. When times are good, property development is a good bet. The rising tide of **China Inc.** raised all boats, particularly around the Pearl River Megalopolis of Guangdong Province-Hong Kong-Macau. In fact, property investment has been such a good deal everybody uses it as collateral. It is the ultimate safe store of value…when times are good. And, because of that it backs a large part of China's financial structure.



Rates of return – Bank deposit interest rates are set by Beijing [PBOC] and have been 0.35% since, roughly, 2013. Food inflation was 7.9% year over year at SEP 2020. See a problem here? This means the average consumer can't match his/her savings rate to price increases and must accordingly find more remunerative [read: riskier] places to put their money. It's been that way at least since…well…2013. Hence shadow banking. Shadow banking centers around Wealth Management Products (WMPs). These are issued by banks, trusts and securities firms and are financial products that have a higher monetary return than depositing your money in a bank. While they are sold by financial institutions, they don't appear on the firms' books. This means no deposit regulations. It also means no guarantees. Read: Riskier

What do WMP consist of, you ask? Sometimes property deeds. Sometimes mortgages on property. Sometimes loans against property mortgages. Sometimes stocks collateralized by loans collateralized against mortgages underwritten by your uncle Fred on a Tuesday but only during full moon. Well, maybe not that bad, but far worse than the Collateralized Mortgage Obligations (CMO) that drove the 2008 financial collapse in the US. Yep. Worse.

So what does this have to do with the Evergrande Group. When they started Shenzhen was a muddy field.



This is what it looks like today. Evergrande Group made a lot o'money taking 1980 Shenzhen to 2019 Shenzhen.

So what's the problem? It's not just that Evergrande Group is the largest most indebted company in the PRC. It's not just that its' properties, bonds, stock….paper….are used as collateral for a great deal of the licit banking system. It's not just that Evergrande Group's paper is used in WMPs in the shadow banking system. It's the offshore bond trade.

Evergrande highlights the risks in China's offshore bond trade: Financial Times [Paywall]: Henny Sender: 15 OCT 2020: The Shenzhen-based Evergrande group is too big to fail. "It is so intertwined with the country's banks and financial system that it would be too much of a broader danger to the economy if it defaulted on its $120B of debts. And it is not just a question of the size of Evergrande's borrowings. Its debt is widely held, circulated through shadow banks into retail hands through wealth management products, as well as sitting on bank balance sheets."

"Evergrande's sheer size and extensive liabilities mean its collapse would be a systemic risk to China," said analysts at Gavekal. "The firm's 'too big to fail' status illustrates the balancing act the government faces as it tries to press developers to get their finances in order while avoiding defaults that would ripple through the Chinese economy."

"But investors in the offshore debt of Evergrande should be wary. Much of the Evergrande risk is not in China — it lies instead in the offshore dollar bond market, where junk-rated mainland property groups raise money without the need for approval from Beijing and account for $210bn of the $270bn outstanding there, according to ANZ bank."

"That market has become especially attractive both for issuers and investors in a world where central banks in developed nations have driven rates to zero. Issuance slowed to $12bn in the second quarter but soared to $32bn in the third, while the conditions or covenants giving investors comfort reached their weakest level ever, according to Moody's Investors Service."

"Owen Gallimore of ANZ in Singapore said Evergrande was the single biggest borrower in the Asian high-yield dollar bond market, accounting for $23bn in issuance."

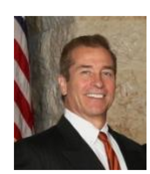
"We think Evergrande is systemically important but you can still treat (offshore) bondholders badly," he said. "Bondholders don't have collateral. They are in a perilous situation. China has learnt with every restructuring to deal more aggressively with bondholders."

So why does Dr. Evil care about some property ponzi scheme in Putang? [Henan Province]. He doesn't. Dr. Evil hopes it crashes and burns along with the PRC's financial system. Dr. Evil is, of course, evil. What did you expect? Dr. Evil is concerned that the PRC is smart enough to export its' upcoming financial debacle to yield hunger western investors abetted by the American Comprador class at Goldman, HSBC and the like. Evergrande's eventual collapse [what goes up, eventually goes down] may take a substantial portion of the western financial system with it. [think 2008] What does Dr. Evil recommend? Start squeezing Evergrande paper off US markets. Remove it as an insurable asset from the Pension Benefit Guaranty Corporation's insurance by regulatory 're-interpretation'. No muss, no fuss.

What does this mean? The Dept. Commerce's PBGC insures defined benefit plans – private sector single and multiemployer pension plans. These are the plans that pay pensioners a certain amount, typically monthly. If the plan goes belly up, the PBGC takes it over and guarantee's the payout. [Well, we're talking about the government here…so kinda] Federal types don't have to worry, Uncle Sam's got your back. [Rrrright] But, if the PBGC strikes dodgy PRC paper from being insured – inside of a US private sector pension plan- this resonates across the universe of 'investment fiduciaries'. Fiduciaries are defined section 3(21)(A)(ii) of the Employee Retirement Income Security Act of 1974 as rendering "investment advice" to an employee benefit plan. If it becomes regulatorily unfashionable to dabble in dodgy paper, fewer people will.

Dr. Evil would like to extend the cold clammy hand of friendship to the evil minions of evil at the Securities and Exchange Commission, who take Dr. Evil missives into the bathroom and read them where they think no one can see them.

Of course we can see them. We're Dr. Evil. But we don't want to see them.



Dave "Dr. Evil" Katz, J35TNT/CTF USSOCOM Contractor