Hong Kong court liquidates failed Chinese property giant

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After protracted negotiations, aimed at trying to restructure its international debts, the failed Chinese property and real estate giant Evergrande has officially been wound up.

The decision was announced yesterday by a Hong Kong court following the failure of a stay of execution in December to produce a solution which satisfied the company's international creditors.

Issuing the liquidation order, High Court judge Linda Chan said: "It would be a situation where the court says enough is enough. I consider it appropriate for the court to make a winding-up order against the company, and I so order."

A restructuring plan, which involved a series of complex negotiations, was on the verge of being agreed to last September but fell through when regulatory authorities failed to grant approval for actions by the company necessary to make it work.

A few days later, Hui Ka Yan, the company's founder and chair, was placed under "mandatory measures" on suspicion of "illegal crimes." No details have been released but the issue is believed to involve the transfer of money abroad.

The effect of the court decision is that it allows a liquidator to take control of Evergrande's assets outside of China. But apart from opening the way for other lawsuits it is not clear what its practical implications will be for the Chinese mainland, where most of the $300 billion worth of Evergrande's liabilities are located.

Judge Chan rejected a request for another adjournment from the company's lawyer, who said an immediate liquidation order would affect the value of the company's offshore assets and its subsidiaries and would be damaging for creditors. But a lawyer for the main group of creditors said the company had not negotiated with them in good faith and the judge agreed.

Rejecting the request for a further adjournment, Judge Chan said Evergrande was "still insolvent" and there was "still no viable restructuring proposal."

Fergus Saurin, a lead lawyer for the creditors, said he was not surprised at the outcome as it was a product of the company's "failing to engage with us."

"There has been a history of last-minute engagement which has gone nowhere. And in the circumstances the company only has itself to blame for being wound up," he said.

The still unresolved issue is how far the wind-up will go. The Hong Kong ruling could open the way for the liquidator to seize Evergrande assets in mainland China. There is an agreement on insolvency and restructuring. But as the *Financial Times* (FT) noted, "it is not clear that mainland courts would accept the Hong Kong winding-up order."

The decision, which will be closely watched, has major implications. There is no precedent for a company the size of Evergrande to be wound up by a Hong Kong court. As an article on Bloomberg noted, "an unfavourable outcome for foreign investors risks exacerbating the acute pessimism toward China as well as undermining Hong Kong's role as a vital fund-raising centre for the nation's companies."

Apart from the immediate issues of the wind-up, there are the longer-term implications for the whole Chinese property and real estate market, which is mired in an ocean of debt.

As the FT commented, the ruling "opens a new and unpredictable phase in the collapse of the world's most indebted property developer." Since Evergrande first defaulted on its international debts in 2021, a series of companies have gone under.

The *Wall Street Journal* described it as a "watershed moment for the Chinese real estate industry and fueled a liquidity crisis in the sector," noting that since then more than 50 developers have defaulted on their debts and thousands of people had lost their jobs.

Real estate and related industries "used to be a major driver for the country's economic growth and contributed to around a quarter of its gross domestic product" but now it is dragging down the economy and looks like it will continue for years.

"New data on the sector's 2023 performance showed a desperate picture, and economists say the downturn—now in its fourth year—is about to get worse," the report continued, citing data which showed that the sales of new homes in China fell by 6 percent last year to a level last seen in 2016.

While the flow-on effects of the Evergrande liquidation are not yet clear, it will no doubt make the efforts of the government to halt a stock market rout more difficult.

After previous measures to curb the falls had failed, regulators yesterday announced measures to limit short selling. This is the practice in which market players borrow shares they do not have and sell them in the expectation that their prices will fall, whereupon they buy them at the lower price and return them to the lender, making a profit on the transaction.

The Shanghai and Shenzhen stock markets announced that investors who buy shares will not be allowed to lend them out for short selling within a specified lock-up period.

The China Securities Regulatory Commission said the restrictions were intended to "create a fairer market order" and foreshadowed further restrictions on the lending of securities in March.

Last week China's premier Li Qiang said there would be "more forceful" state support for the market, which is undergoing a steep decline. But after a three-day rally, the market started to fall again on Friday.

The CSI index, which covers the Shanghai and Shenzhen markets, fell 11 percent last year, its third consecutive annual decline, and Hong Kong's Hang Seng index was down 14 percent for the year, its fourth consecutive annual fall.

Since reaching their peak in 2021, Hong Kong and mainland markets have lost $6 trillion in value, more than the market value of the Tokyo stock exchange.

The restrictions on short selling are expected to have a very limited impact if they affect the market at all.

As numerous commentators and analyists have pointed out, the main issue is lack of confidence in the direction of the economy.

At the beginning of last year there was a flow of international capital into the Chinese markets in the belief that the lifting of anti-COVID public health measures would provide a boost to the economy. But the uptick was short-lived.

It has been estimated that of the $33 billion which flowed into the market from foreign investors, 90 percent had been withdrawn by the end of the year. Apart from the failure of a sustained upswing to materialise, another contributing factor in the fall of the market was the insolvency of the property developer Country Garden, which had been previously touted as being free of the problems besetting Evergrande.

It is too early to say yet, but the formal liquidation of Evergrande may well add to the fall in the stock markets and set off turbulence in other areas of the financial system as well.