

# THE WALL STREET JOURNAL.

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February 15, 2002

## Strategy Revealed in Collapse of Chinese Investment Trust

### Beijing Forces Fujian Trust Into Ranks of Defaulters Amid Financial Cleanup

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BEIJING—The recent collapse of another Chinese investment trust company, which leaves angry U.S. and Japanese bondholders in its wake, highlights China's strategy of forcing write-offs of past financial problems even at the risk of tainting current investor sentiment.

Unlike many of its highflying counterparts, Fujian International Trust & Investment Corp. was supposed to be different. It steered clear of the speculative property investments and loans to poorly run state companies that characterized other Chinese trusts and banks swollen with bad debts. Instead, the Fujian company opted for safer bets like stakes in utilities and airlines, and foreign investors extended it some \$200 million in credit through Yankee and Samurai bonds. But after the closing of its doors in December, and missing a Samurai payment on Jan. 24, Fujian Trust has been lumped with its debt-defaulting counterparts.

Paradoxically, the closure is driven by motivations that most foreign investors

would applaud: A sweeping financial cleanup that is quietly gathering speed. After the collapse in 1998 of the Guangdong International Trust & Investment Corp., known as Gitic, Beijing slashed the number of such companies to about 60 from 240. As part of the cleanup, the central government disavowed the sector's foreign debt, officially estimated at \$12 billion. Though the move angered creditors, analysts praised the attempt to draw a clear line between the central government's credit and that of corporate borrowers. It also helped China preserve an investment-grade sovereign rating, even as an assortment of Chinese corporate bonds slid to junk status.

"From our narrow perspective, it reinforces what is 'sovereign' and what is not," said Joydeep Mukherji, a director with Standard & Poor's sovereign ratings group.

But the termination of Fujian Trust has offered a reminder of the risks for creditors amid China's untidy economic reforms. Because the company still had years to pay the principal on its foreign bonds, and several worthy investments, creditors suspect the Fujian provincial government sought to sidestep the company's obligations and blame an industry consolidation for the closure.

That perception has been bolstered by the image of Chinese companies in overseas credit markets, battered by a string of questionable defaults. "It bothers me a great deal when you have to question the

### Issues of Trust

Prices of distressed and high-yield bonds for Chinese trusts, as a percentage of face value or in cents on the dollar, and whether payments are current

ISSUER	PRICES			
	Feb.-March 2001	Nov. 2001	Feb. 2002	Current
Guangdong ITIC	12	16	15	No
Tianjin ITIC	32	91	100 <sup>1</sup>	Yes
Fujian ITIC	37	70	49	No <sup>2</sup>
Hainan ITIC	23	28	28	No

<sup>1</sup>Redeemed at par at the end of 2001

<sup>2</sup>Missed Samurai payment due Jan. 24; Yankee Bond payment due Feb. 25

Source: Exotix

institution's willingness to pay," said Fan Jiang, an executive director for fixed income at Goldman Sachs in Hong Kong. "The easiest thing to do for a borrower is to raise your hand and say 'I default.'"

The closure caught bondholders off-guard, as it came before both the payments on the Samurai and the Yankee bond were due. "I think mainly what they saw was a narrowing window of opportunity where they might be able to slip in there with their own little tactical default

when nobody was looking," said David Boren of Montpelier Asset Management, a London based investment firm, which holds "substantial" holdings of the company's bonds.

An official reached at Fujian Trust, who declined to be identified, said the decision to close the company was made by the Chinese central bank, not the provincial government. He refused to answer other questions, such as the size of debts and plans for repayment. As it did with the January Samurai payment, the Fujian company is expected to miss a Feb. 25 Yankee bond payment. But creditors complain that a grace period on the U.S. debt gives them just two weeks to register claims. Now, both sets of creditors are preparing for negotiations with the government to recover as much as they can from the 14 billion yen Samurai, which expires in 2006, and the 10-year \$100 million Yankee bond, which falls due in 2007.

In moving to shutter a troubled trust, Fujian is hardly the first to cite orders from the top. Aside from Gitic, investment trusts in Guangzhou, Hainan province and the northeast city of Dalian have struggled to repay foreign obligations. Another, the municipality of Tianjin, initially announced difficulty with its Japanese debt, before repaying bonds and loans last year amid diplomatic negotiations between the Chinese and Japanese governments, say bond industry executives.