

Unsold corporate bonds may hit a record-high in seven years

Institutional investors are becoming wary of investing in Korean corporate bonds due to uncertainties caused by the coronavirus. As of July 20, there were in total 1.30 trillion won (\$1.08 billion) worth of unsold corporate bonds in the market, according to Market Insight, a capital market news outlet from the Korea Economic Daily.

Unsold corporate bonds have reached a new high since posting 773 billion won in 2017. At this rate, it is expected to reach the highest level in seven years if it surpasses the record of 1.96 trillion won in 2014, and 1.37 trillion won in 2016. In 2013, unsold corporate bonds hit the highest record of 7.63 trillion won.

Unsold corporate bonds reached a historic high in 2013 when the now-defunct Tongyang Group's financial unit Tongyang Securities sold risky bonds to more than 40,000 individual investors to secure liquidity for the cash-strapped group. The group eventually filed for court receivership without being able to pay off its debt, resulting in a hefty amount of loss among investors. This made investors avoid corporate bonds, especially from companies that had poor credit ratings.

So far this year, 17 companies including Hanwha Solutions, Hanwha Engineering & Construction, GS E&C, KCC, and HDC Hyundai Development Company among others failed to reach the target amount in the bookbuilding process. Among the 17 companies, 12 had lower than AA- credit ratings.

“Many companies are issuing bonds with a higher than average yield - with the exception of companies that have good credit,” said an industry banking source. He

explained that these circumstances are unlikely to change as long as the global pandemic continues, given that it is the reason behind weakened investor sentiment.

Since April the government has released a range of stimulus measures including a bond market stabilization fund, Korea Credit Guarantee Fund's primary collateralized bond obligation (P-CBO), along with state-lender Korea Development Bank's purchasing of corporate bonds and a special purpose vehicle to purchase low credit corporate notes.

However, these measures have not been so effective. Only corporate bonds with higher than AA-credit rating are seeing slight improvement whereas corporates with lower credit are still struggling to find a way for financing.

Institutional investors are hesitant to invest in companies with a high-risk potential, even if they have a healthy balance sheet.

For example, HDC Hyundai received only 11 billion won from the bookbuilding conducted on July 6, far below its target of 300 billion won. This is due to concerns that the company's financial structure may suffer once its acquisition of Asiana Airlines is finished.

In November 2019, HDC Hyundai announced plans to acquire the country's second-largest flag carrier Asiana Airlines for approximately \$2 billion. The deal was originally intended to wrap up by June, but it has faced some turbulence due to the coronavirus impacting the debt-laden carrier and the overall airline industry. Amid speculation that HDC Hyundai may drop the deal, the airline carrier's creditor Korea Development Bank requested the company to confirm that it will proceed with the acquisition.

HDC Hyundai Development has confirmed that it will remain committed to the deal but asked to revisit the terms given that Asiana Airline's debt ratio has increased by 16,126% compared to the second quarter of 2019 due to the global pandemic.

HDC Hyundai has posted a negative net debt for several years, and its first-quarter operating profit was 137.3 billion won, a 35.2% year-on-year increase.

Corporates planning to issue new bonds are becoming more anxious as there is a high chance that underwriters may not be willing to take on unsold corporate bonds. Underwriters need to dispose bonds when their book limit is full, which means that they may have to sell off bonds at a bargain price in the retail market.

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