# Corporate Strategy by Peter Rush

## Hong Kong real estate over the edge

*Sooner or later, depending on the Hongshang, the world collapse will wipe out the island's scams.*

Information made available to *EIR* belies the recent spate of assertions that an unravelling of Hong Kong's entire financial structure has been averted.

The real-estate bubble consisted of a quadrupling of property prices between 1978 and the end of 1981, based on a 70 percent annual growth of credit injected from the unregulated banking and investment sectors. As revealed by the *Far Eastern Economic Review,* the actual situation is an amazing tangle of leveraged properties, cross-holdings, buy-back arrangements, interlocking deals, back-scratching arrangements and related practices. The result is that a lot of individual investors and a lot of foreign banks have dumped a great deal of money into Hong Kong, and it will now be interesting to see how much of it they ever get back out.

Perhaps the most blatant operation to surface so far is the case that touched off the recent panic, the Nov. 17 insolvency of Dollar Credit & Financing Ltd. It now emerges that Dollar Credit, which disclosed Nov. 15 that it couldn't pay its debts, amounting to HK$650 million had HK$560 million in loans, two-thirds of its entire loan portfolio of HK$864 million, secured by nothing but the personal guarantee of F. S. and J. Mao. $278 million of that sum had been lent to the two gentlemen days before the announcement of insolvency. It now appears that J. Mao is a director of Dollar Credit's parent company, through which influence, presumably, he was able to run the entire scam. Burned in the affair, among 39 major creditors, are Crocker National Bank in San Francisco, which has secured a court order freezing Dollar's New York deposits, and American Express International Banking Corporation.

Then there are the operations of the Carrian Group, which includes a public stock company and several private companies, and a host of miscellaneous subsidiaries. The public company has HK$3 billion in deferred liabilities and $4.1 billion in stockholders' funds (book value), but apparently a very tiny equity base, most likely under $500 million. (There are approximately seven Hong Kong dollars to one U.S. dollar.) Until recently, Carrian's primary source of revenue was windfall capital gains from quickly reselling certain properties at a huge markup. With real-estate values now at half what they were a year ago, this source of income is gone forever.

Finally, the post-1981 fall in Carrian shares, beginning before any problems had been made public, strongly suggests that the non-Hong Kong resident Chinese backers of the company made a stock killing, and then got out. Paribas, Barclays, and the PRC's Bank of Communications are among those holding the bag now.

The third of the troika is Eda Investments Ltd., all but one of whose creditors have just agreed to disastrous terms of debt rescheduling. Against HK$1.4 billion in debts, the company has only $475 million in assets, down from $847 million in Sept. due to the real estate collapse. The agreement will provide only $12 million annually in interest payments against the $1.4 billion in debts.

Information provided *EIR* shows that much more may be about to blow: several very large real-estate firms engaged in building new buildings will be clobbered if real-estate prices don't rebound soon. Calculations of "worst-case" liquidity problems by a knowledgeable New York firm show that if no revenue comes in from capital commitments (selling or leasing of new properties), and existing payments are maintained, several major firms would be short, collectively, by many billions. Hong Kong Land, one of the largest firms, would find itself short by HK$7.3 billion (95 percent of its marketable assets); Hang Lung would be short HK$554 million (77.7%); Su Long Kai, HK$1.4 billion (69.9%), and Hong Kong Wharf HK$1.1 billion (26%), among others.

Every expectation that this crisis won't hit depends on a near-term recovery. This is a chimera. The foreign banks, already burned, are looking for the nearest exit. The stock market has already fallen more than 50 percent.

Ultimately, it was demand for new office space that made the boom possible. Now, over-capacity is already severe, with many office buildings under construction yet to hit the market. The plummeting of world trade and the general depression ensure there will be no revival of office-space demand—all of which means that the real-estate market is heading further down. And this will burst the Hong Kong bubble—sooner, if the Hong Kong and Shanghai Bank walks away; later, if Hongshang makes a serious effort to stem the collapse by means of massive capital infusions, instead of the small ones thus far supplied.